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90-81

No. . . . .

Supreme Court, U.S.
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JUN 28 1990
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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1990

W. DAVID WESTON
Petitioner/Appellant

V.

JEFFREY G. BANKS, ET AL.
Defendarts

On Writ of Certiorari to the United States Circuit Court of Appeals For the Tenth Circuit

APPELLANT APPENDIX "A - 2" DISTRICT COURT AMENDED FINDINGS INTERLOCUTORY JUDGMENT

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BEST AVAILABLE COPY

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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1990

W. DAVID WESTON
Petitioner/Appellant

v.

JEFFREY G. BANKS, ET. AL.,
Defendants

PETITION FOR WRIT OF CERTIORARI

AMENDED FINDINGS OF FACT AND CONCLUSIONS OF LAW OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH CENTRAL DIVISION IN CASCADE V. BANKS

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH
CENTRAL DIVISION
No. C-82-1223C

CASCADE ENERGY AND METALS CORPORATION,
a Nevada corporation,

Plaintiff,

v.

JEFFERY G. BANKS, et al,

Defendants

JEFFERY G. BANKS, ET AL,

Counterclaimants, Cross-laimants, and
Cross-Counterdefendants,

vs.

CASCADE ENERGY-AND METALS CORP.,

Counterdefendant and
Cross-Counterclaimant,

and

W. DAVID WESTON, TELEGRAPH MINE LIMITED, a partnership, REX MONTIS SILVER CO., TELEGRAPH MINE JOINT VENTURE, GOLD TECHNICS, LTD., a limited partnership, INTERPHASE CORP., JAMES F. PETERS, as TRUSTEE of the GNOLAUM UNITRUST,

Cross-Counterclaimants and
Cross-Defendants

Bradley H. Parker, Esq., of Parker, McKeown & McConkie, Salt Lake City, -Utah, for plaintiff, counterdefendant and cross-counter- claimant Cascade Energy and Metals Corp.

Dennis F. Olsen, Esq., of Olsen & Associates, Salt Lake City, Utah, and Richard A. Love, Esq., Santa Monica, California, for defendants, counterclaimants, cross-claimants and

cross-counter-defendants Samuel Harmatz, Bernard Hodowski, Harmatz and Hodow-ski, a California partnership, H. E. Moses, Chris Waugh, A. C. Nejedly.R. E. Donahey, Grace V. Duncan and Elliot Weinberg.

George M. Haley, Esq., of Haley & Stolebarger, Salt Lake City, Utah, and Thomas L. Watters, Esq., Santa Monica, California, for defendants, counterclaimants, cross-claimants and cross-counter defendants Jeffery G. Banks, Kenneth Caldwell, Coastal Computer Investments, a California partnership, Elmer J. Davis, David G. Henry, Roger A. Mann, Mann Caldwell Partnership, Robert A. Nickerson, Peter P. Samarin, Patricia Stoltenberg, Herbert W. Stoltenberg, Edwin Stoltenberg, Delford Ashley, George Slater, Patricia Slater, Robert Doub, Sam Hambarian, AlyceHambarian, and Lionel Ascher.

Richard N. Bigelow, Esq., Salt Lake City, Utah, for cross-counter- claimants and cross-defendants W. David Weston, Telegraph Mine Limited, a partnership, Rex Montis Silver Co., Telegraph Mine Joint Venture, Gold Technics, Ltd., a limited partnership, Interphase Corp., and James F. Peters, as Trustee of the Gnolaum Unitrust.

William H. Orton, Esq., amicus curiae on behalf of non-party investors in connection with consideration of amendments to findings of fact.

CHRISTENSEN , J.

This case was tried to the Court beginning October 9, 1984, and continued from day to day with brief recesses to and including October 31, 1984, when it was submitted for decision on the evidence, the oral arguments of counsel, written briefs and proposed findings of fact and conclusions

of law suggested by counsel for the respective parties, all of which were duly considered. On March 1, 1985, the Court filed its Findings of Fact and Conclusions of Law with an invitation to counsel to suggest changes, if any, for their better conformity to the record. Various changes were suggested which were considered on March 26, 1985, after notice, together with changes discussed by the Court sua sponte, argument of amicus curiae who had been granted leave to be heard in behalf of non-party investors who might be affected although not bound by the Court's determinations, the forms of judgment to be entered, and preparations for the accounting to be thereby ordered.

Now deeming itself to be fully advised, the Court makes and enters the following

AMENDED FINDINGS OF FACT

I. STATEMENT OF THE CASE

I-A. General

1. Plaintiff filed its action against the defendants on December 17, 1982, claiming damages in contract and tort in connection with its services as operating manager of property known as the Telegraph Mine under contract with the owners of working leasehold interests in the mine, defendants herein(Defendant Associates). Certain other owners of workingleasehold interests in the mine are not parties, having nodifferences, or having resolved any difference with the plaintiff at least for the present.

I-B. Parties and Jurisdiction

2. The plaintiff was and is a corporation organized and existing under the laws of the State of Nevada and maintain-

ing its principal place of business in the State of Utah. The Defendant Associates were and are citizens of states other than the states of Utah and Nevada, principally from the State of California, and there existed at the commencement of the action and during all material times complete diversity of citizenship between the plaintiff on the one hand and the defendants on the other. The amount involved in each and all aspects of the actionis in excess of 510,000.00 exclusive of interest and costs. Subsequent to the filing of plaintiff's complaint, additional defendants were added with leave of court, all of whom were andare citizens of states other than Nevada and Utah, and compulsory counterclaims and cross-counterclaims between and among the defendants, the plaintiff, and other parties brought into the case in connection with said counterclaims and cross-counter- claims, were filed, over all of which the Court had and has ancillary jurisdiction as well as primary jurisdiction by reason of their being claims arising under the securities laws of the United States and claims pendent thereto.

3. The Court acquired complete personal jurisdiction by due and legal service-of process or voluntary appearances. Venue in this court was and is proper under governing rules and law, and most convenient for resolution of all related disputes between and among the parties.

4. The plaintiff Cascade Energy and Metals Corporation (Cascade) is a publicly held corporation, of which W. David Weston (Weston) during all material times was president, a member of its board of directors, the beneficial owner of a controlling stock interest in the corporation and acting within the scope of his authority from the corporation.

5. Rex Montis Silver Company (Rex Montis is a publicly held corporation formed under the laws of the State of Utah, of which Weston during all material times beneficially owned or controlled at least thirty-three percent of the

outstanding stock and was the president and a member of the board of directors and for which he was acting within the scope of his authority Rex Montis was formed in 1969 as part of a reorganization of a California corporation known as Rex Montis Company, of which defendants and counterclaimants Harmatz, Hodowski, Waugh,Donahey and Stoltenberg were shareholders.

6. Telegraph Mine Limited during all material times was and is a partnership controlled by Weston, with Cascade as its general partner.

7. Interphase Corporation (Interphase) was and is a Utah corporation and during all times material herein wasprincipally owned and solely controlled by Weston and performed, among other things, accounting services for Cascade and other entities with which Weston was connected. The Gnolaum Unitrust (Gnolaum Trust) during all times material herein was and is a revocable trust established by Weston for the benefit of his family, of which James F. Peters was the trustee.

8. Gold Technics, Ltd. (Gold Technics) was originally a California corporation known as Gold Technics, Inc. Thereafter, it was reorganized as a California limited partnership with Bernard Hodowski, Samuel Harmatz and Weston as general partners and a number of the cross-claimants and cross-counterdefendants as limited partners (Gold Technics Defendants).

I-C. Issues

9. Plaintiff's first amended complaint contains seven claims for relief: (1) breach of contract;.(2) quantum meruit; (3) breach of quasi contract; (4) breach of fiduciary duty; 15) tortious interference with prospective economic gain; (6) tortious interference with business; and (7) tortiousinterference with contracts. Claims 1, 2 and 3 arose out

of the contractual obligation plaintiff claimed defendants assumed by the Joint Operating Agreement for assessable costs and expenses beyond development and royalty notes signed by the investors. Claim 4 was for alleged breach of fiduciary duties againstHarmatz, Hodowski, Waugh, Donahey, Moses, Nejedley, Duncan and Weinberg for allegedly seeking to financially undermine the project for their personal gain. Claim 5 was against defendants Harmatz, Hodowski, H. Stoltenberg, Waugh, Donahey, Moses, Ascher Nejedley, Duncan and Weinberg for alleged tortious interference with plaintiff's prospective economic gain by reason of its ownership of a sublease working interest and contractual interest in all production at the Telegraph Mine. Claim 6 was against Harmatz, Hodowski, Waugh and H. Stoltenberg for alleged tortious interference with the business relationships of plaintiff as an owner of a sublease working interest and as operating manager of the Telegraph Mine by virtue of an alleged conspiracy totortiously interfere with the business relationships between the plaintiff and others. Claim 7 was against Harmatz, Hodowski, H. Stoltenberg and Waugh for alleged tortious interference with plaintiff's contract as operating manager for the Associates in the Telegraph Mine Associates' Project.

10. The investor defendants denied the materialallegations of plaintiff's first amended complaint, alleged that plaintiff made material misrepresentations and omissions of fact upon which defendants relied when entering into the contractual relation- ships with plaintiff and that the agreements were subject to rescission as procured by fraud and for other reasons and that they had been rescinded. Defendants allege that the interests were sold to them in breach of federal securities laws and California state securities laws; that any communications they. had with other investors were privileged, true and without malice and that any interference with contractual relationships was

justified. Defendants further alleged that the agreements were contracts of adhesion and contained unconscionable terms,including minimum annual royalty payment requirements of$2,600,000.00 annually.

11. Defendant Associates "first amended cross claim and third-party complaint" was against the plaintiff and W. David Weston, Telegraph Mine Limited, Rex Montis Silver Company, Gold Technics, Ltd., Telegraph Mine Joint Venture, InterphaseCorporation, James F: Peters as Trustee of Gnolaum Unitrust and 1000 Does, claiming rescission, restitution and damages based on alleged misrepresentation, fraud, breach of contract, violation of the federal and California securities acts, breach offiduciary duty, fraud and conversion, and for declaratory,equitable and injunctive relief.

12. The plaintiff and others as counterdefendants filed an answer generally denying the allegations of the counterclaim, raising as defenses accord and satisfaction, assumption of risk, estoppel, failure of consideration, fraud, illegality, injury by a fellow servant, laches, license, payment, res judicata, stature. of limitations, in pari delicto and waiver, and alleging that counterclaimants were sophisticated investors who assumed the risk of the investments and represented to the Internal Revenue Service that they were sole proprietors in the Telegraph Mining Associates Project. The plaintiff and other counterdefendants alleged by way of counterclaim against the defendants Harmatz, Hodowski, Waugh, H. Stoltenberg, E. Stoltenberg, Moses, Banks, Donahey, Nejedley, Duncan and Weinberg that they were co-promoters of the sales of sublease working interests in the Telegraph Mine Project and were jointly liable for any damage allegedly caused by plaintiff and 'third-party defendants' and that said defendants were estopped because of this relationship.

13. The Gold Technics Defendants, by way of answer

to the counterclaims against them and by adopting various responses of the other defendants, claimed truthfulness, accuracy and privilege for any alleged defamatory statements or other claimed tortious conduct, alleged that plaintiff was barred from any recovery due to the plaintiff's breach of fiduciary duty and fraud with regard to the Gold Technics Defendants and further asserted that plaintiff wasTechnics Defendants and further asserted that Plaintif f was barred from relief under the doctrines of unclean hands, laches, failure of consideration and failure to join indispensable parties.

14. The Gold Technics Defendants filed a separate counter- claim against plaintiff, Rex Montis, the Telegraph Mine Limited,, Gold Technics, Ltd., the Telegraph Mine Joint Venture, W. David Weston and Interphase as counter-defendants forrestitution and damages following alleged rescission of aSeptember 1, 1980, agreement concerning the exchange of 480,000 shares of Rex Montis stock for a thirty-percent ownership in the Telegraph Mine, breach of fiduciary duty by Rex Montis as a general partner of Gold Technics, Ltd., for failure and refusal to rescind the September l, 1980, agreement, and for declaratory relief concerning the rights, duties, liabilities and responsibilities of Rex Montis and Gold Technics, Ltd., under the September 1, 1980, agreement, for an accounting of Gold Technics, Ltd. and Rex Montis as general partner of Gold Technics, Ltd., for an accounting by the Telegraph Joint Venture and Cascade and Rex Montis as the Telegraph Joint Venture manager and Telegraph Joint Venture, respectively, for revenues, profits and assets of the Telegraph Joint Venture, for alleged breach of fiduciary duty in the conversion of assets, overcharging for services and equipment and obtaining secret profits, for damages, for fraud, misrepresentation and concealment in connection with the September 1, 1980, agreement and for the offering of the sale of sublease interests in

and operation of the Telegraph Mine, and for damages for interference with prospective economic advantages. Plaintiff and other counterdefendants filed an answer denying substantially the operative allegations made against them and raising the affirmative defenses of the statute of limitations, failure to pursue administrative remedies,laches, performance, failure to mitigate damages, release of liability, negligence and intervention by others.

15. As if this were not enough, Interphase and Gnolaum Trust filed a counterclaim against the Defendant Associates and Gold Technics Defendants, alleging breach of a Joint Operating Agreement and refusal to pay assessments thereunder, breach of partnership duty in connection with the Joint Operating Agreement, breach of fiduciary duty against Hodowski, Waugh and H. Stoltenberg, fraud against Hodowski, Waugh and H. Stoltenberg arising out of the 'Management Committee,' tortious interference with prospective gain against Hodowski, Waugh and H. Stoltenberg and tortious interference with contracts against Hodowski, Waugh and H. Stoltenberg.

16. Counterdefendant Telegraph Mine Joint Venture, filed an amended counterclaim against the investor defendants and Gold Technics Defendants for alleged breach of sublease agreement for failure to pay minimum annual royalties and assessments, breach of Joint Operating Agreement for failure to repay a loan, breach of subcontract for refusal to pay various amounts, to declare defaults under sublease agreement, breach of fiduciary duty as to Gold Technics Defendants, tortious interference with prospective economic benefits against Harmatz, Hodowski, Waugh, Moses and H, Stoltenberg, tortious interference with business relationships as to Hodowski, Harmatz, Waugh and H. Stoltenberg, and tortious interference with contracts as to Hodowski, Harmatz, H. Stoltenberg, Waugh and Moses.

17. An amended counterclaim of Rex Montis against

the Defendant Associates and the Gold Technics Defendants was for alleged breach of the Telegraph Mine Lease Purchase and Joint Venture Agreement against the Gold Technics' Defendants, breach of the Gold Technics/Rex Montis purchase agreement against the GoldTechnics Defendants, breach of the Telegraph Mine and Joint Venture Management Agreement against Gold Technics Defendants, breach of sublease agreement against Gold Technics Defendants, breach of fiduciary duties against Gold Technics Defendants, tortious interference with prospective economic benefits against Harmatz, Hodowski, Waugh, Moses and H. Stoltenberg, tortious interference with business relationships against Harmatz, Hodowski, Waugh and H. Stoltenberg and tortious interference with contracts against Hodowski, Harmatz, H. Stoltenberg, Waugh and Moses.

18. The counterdefendant Telegraph Mine Limited, filed an amended counterclaim against the investor defendants and Gold Technics Defendants for breach of the Telegraph Mine LeasePurchase and Joint Venture Agreement against Gold TechnicsDefendants, breach of the Telegraph Mine Venture Management Agreement against Gold Technics Defendants, breach of sublease agreement against Gold Technics Defendants, breach of fiduciary duties, tortious interference with prospective economic benefits against Hodowski, Harmatz, Waugh, Moses and H. Stoltenberg, tortious interference with business relationships againstHodowski, Harmatz, Waugh and H. Stoltenberg, tortiousinterference with contracts against Harmatz, Hodowski, H.Stoltenberg, Waugh and Moses, and for declaratory relief regarding Gold Technics' purchase of its interest in the Telegraph Mine prime lease.

19. An additional counterclaim was filed by Rex Montis, Telegraph Mine Limited, Telegraph Mine Joint Venture, Weston, Interphase and Cascade for declaration of rights

regardingcontracts with Gold Technics Defendants, breach of fiduciary-duties by Gold Technics Defendants, quantum meruit recovery against Gold Technics Defendants, fraud against Gold Technics Defendants, breach of agency against Gold Technics Defendants, tortious interference with contracts against Gold Technics Defendants and for contribution against Gold Technics Defendants.

20. Defendant Associates and the Gold Technics Defendants have filed answers to the additional counterclaims generally denying the allegations thereof and raising the affirmative defenses of the statutes of limitation, lack of subject matter and in personam jurisdiction, truth, privilege and absence of malice, justification, estoppel and laches, failure of consideration, the absence of necessary parties and the failure properly to align the parties and that the counterclaims were filed without leave of court and should be stricken. Indeed, all of the claims made by the various parties have been broadly denied and countered by all others involved and such adversity maintained so that aside from limited background facts largely of a neutral nature, everyone contests everything as it were. All of the charges and countercharges are intertwined and convoluted, rendering it difficult as a practical matter to consider part of them without considering all. And all claims and defenses arise out of a common nucleus of facts, although separate, distinct or ancillary in varying degrees and in various respects. It seemed imperative, in any event, that they should be resolved as far as possible in a single action, without further fragmentation or complication among multiple courts and jurisdictions in which they were being pursued when an effort was made to consolidate the claims here. It is understood that numerous actions are pending in various states involving the same subject matters and, dependent upon the outcome here, numerous others are contemplated.

21. An attempt was made to mercifully merge these pleadings into a pretrial order which, after considerable discussion among counsel and urgings toward simplification by the Court, was finally agreed upon by the parties and entered on September 17, 1984. The recitation of uncontested facts in this pretrial order is incorporated herein by reference, although to add context to these findings some of them are reiterated expressly. The hope for simplification of the issues, however, proved a forlorn one, since each of the parties held tight to almost every claim or defense referred to in the pleadings.

II. BACKGROUND AND SUBSIDIARY FINDINGS

II-A. Genesis of Offering - The Telegraph Mine

22. Several years prior to the time of the hereinafter discussed developments critical to this case, Harmatz, Hodowski and Waugh had been associated with Weston in connection with the affairs of Rex Montis. They became mutually interested in possible development of the Telegraph Mine hereinafter more particularly described. The change in organization of Gold Technics from a corporation to a partnership was with a view toward spreading income which Weston, Hodowski, Harmatz and Waugh hoped Gold Technics would realize as a result of their further association in the development of that mine.

23. The Telegraph Mine consisted of numerous mining claims located in San Bernardino County, near Baker, California, which had been mined periodically from 1932 to 1946 with some success in the production of gold. In 1974, Cascade hadacquired the Telegraph Mine for a consideration of $100,000.00, together with the assumption of a government loan outstanding against the property. Then the mine was in disuse and run down among other things be-

cause of the low price of gold, which was controlled by law at $35.00 per ounce. In May 1976 Cascade leased by prime lease the mining rights to Telegraph Mine Limited. The original mine claims were those particularly described as 'The Original Claims' in Exhibit 'E' to the 'First Amended Cross Claim' and Third-Party Complaint'1 on file herein. Other claims listed in Exhibit E' were added to the project throughthe efforts of Cascade after the purchase of undividedinterests by the Associates as hereinafter related.

24. After acquisition of its leasehold interest in the Telegraph Mine, Telegraph Mine Limited contracted to sell a forty-percent interest in its lease to Gold Technics, Inc., predecessor to Gold Technics, Ltd. In January 1979Gold Technics, Inc. and Telegraph Mine Limited entered into 'The Telegraph Mine Lease Purchase Joint Venture Agreement,' whereby for an agreed consideration of $150,000.00 Gold Technics,Inc. acquired a forty-percent interest in the lease and became part of the Telegraph Mine Joint Venture. On that same date, Telegraph Mine Limited, Gold Technics, Inc., and Cascade entered into 'The Telegraph Mine Venture Management Agreement,' whereby Cascade was made operating manager of the joint venture.

25. Subsequently, Harmatz and Hodowski approached Lawrence Williams with the problem of financing development of the mine. Mr. Williams was a California attorney with an extensive background in securities law and with particular experience in preparing offerings for the sale of interests in gold and silver mines. Weston was introduced to Williams by Harmatz and Hodowski. In January 1980 an agreement was reached between Cascade and Williams whereby Williams would prepare an offering Memorandum with supporting documents and file thenecessary documents for limited offering exemptions and permits or registrations with the states in which the offerings were to be made, with a view of selling thirty-five working

interests through subleases in the Telegraph Mine.

26. In May of 1980, when Gold Technics, Inc. was dissolved and the Gold Technics, Ltd. partnership was formed as aforesaid, an 'Agreement Covering Interests in Telegraph Mine' was entered into by Cascade, Telegraph Mine Limited, Gold Technics, Inc., and Gold Technics, Ltd., whereby the rights and obligations of the parties created under the January 1979 agreement were essentially preserved and Gold Technics, Ltd. acquired the rights and liabilities which had previously belonged to Gold Technics, Inc.

27. After being advised of probable adverse taximplications to Gold Technics, Ltd. of its forty-percent interest in the lease of the mine if and when the thirty-five working interests were sold, Gold Technics, Ltd. entered into anagreement with Rex Montis in September 1980, providing that Rex Montis would acquire a thirty-percent interest in the Telegraph Joint Venture (or seventy-five percent of Gold Technics' interest in the prime lease) and become the general partner of Gold Technics, Ltd. Rex Montis as consideration agreed to issue 480,000 shares (restricted) of Rex Montis stock to Gold Technics. The entire agreement was contingent upon the closing of the Telegraph Mine offering. Accordingly, it was contemplated that after the thirty-five working interest and sublease units were sold, the sublessors' interests would be, respectively, Telegraph Mine Limited sixty percent, Rex Montis thirty percent and GoldTechnics ten percent.

II-B. The Offering: The Confidential Memorandum

28. The offering of the sublease and working interests in the mine was accomplished through the use of a "Confidential Memorandum," consisting of various financial projections,geological reports and mining studies, docu-

ments setting out the terms of the offering, the risk factors involved and the tax aspects of the offering, a Joint Operating Agreement, and several other "Execution Documents." Williams had the majorresponsibility for drafting some of these documents, particularly as they related to the broad outlines of the project and its tax aspects, and he collaborated with and made suggestions to Weston on most of the other phases of the documentation, but Weston assumed the leading correlating role and the primary responsibility for the geological interpretations and financial projections, based on the geological reports upon which he relied and to which he referenced. The work of Williams and Weston in its various stages was sent to Harmatz and Hodowski from time to time for their suggestion and approval. With respect to the Joint Operating Agreement, Weston supplied essentially the final draft to Mr. Williams, who then incorporated it into the format of the offering. Indeed, the evidence at the trial disclosed that in 1982, at a time when Weston was trying to persuade the Associates that his interpretation of the contract as to the assessability of their interests was correct and that Williams' reported view to the contrary was not correct, Weston asserted that he, not Williams, knew what the contract provided because he was responsible for its language. Be that as it may, it is clear that Williams' efforts to safeguard the investors' potential tax advantages by providing for their broad individual control and essentially their right to manage the property especially during production phases, permeated its language and contributed to its effect, as finally formulated by Weston who was not an attorney, of essentially placing control in the hands of the investors, as hereinafter more particularly found.

29. The Confidential Memorandum, dated October 1, 1980, which was received in evidence as Joint Exhibit 1, consisted more specifically of a general statement of the

offering, an explanation of the terms, a description of the mining property, the contemplated activities and use of funds, the description of Cascade as operating manager and its compensation, a description of the Joint Venture offering the units and the managing agents of its members, the owners of the prime lease which would become sublessors of the mine to the investors as sublessees, the conflicts of interest among the offering parties and others connected with them, the risk factors to be considered in connection with any investment, a detailed discussion of tax aspects of the investment, explanation of the Joint Operating Agreement among Cascade and the investors and their rights thereunder, reference to the legal opinion of attorney Williams, tables of "Taxable Income and Cash Flow Projections," and instructions for responding to a pre-offering questionnaire. Attached were copies of "Execution Documents referred to in the preceding explanations": Exhibit A, Offeree Questionnaire; Exhibit B, Questionnaire for Offeree Representatives; Exhibit C, Working Interest Agreement and Sublease; Exhibit D, Joint Operating Agreement; Exhibit E, (Recourse) Royalty Note; Exhibit F, Security Agreement; Exhibit G, Geologist Owens' Report and Mine Costs Study attaching the older report of Geologist Tomo Ito which it evaluated and updated, and Exhibit H, Counsel,s Opinion Letter signed by Williams.

30. The summary of the project contained in the Confidential Memorandum referred to the exhibits above enumerated and "documents referred to herein," noting that those not included were available for inspection upon request in the offices of the operating manager. It was explained that each purchaser of units of working interests would enter into the Working Interest Agreement and Sublease effective at the date of purchase and ending when 'all merchantable ore' was mined from the Telegraph Mine. It was the stated expectation, subject to enumerated risk fac-

tors, that significant tax deductions would be experienced in the first year of an individual's acquisition and in taxable income in subsequent years.

31. It was further summarized in the Confidential Memorandum that thirty-five Units of Working Interests were being offered to selected investors with the requisite knowledge and experience to make an informed decision and who could bear the risks involved in the investment. Pursuant to their subleases, each purchaser would pay the sublessors during the term of the sublease royalties of twenty-six percent of gross sales proceeds from minerals extracted from the property but not less than the non-refundable annual minimum royalty of $74,285.00 per annum per unit. The sublease required that the 1980 annual minimum royalty aggregating $74,285.00 be paid $30,000.00 in cash and with a recourse note for $44,285.00, the 1981 annual minimum royalty to be paid in the same manner except for reduction in a "small amount" if the projected production in 1981 should be attained. It was further indicated by way of summary that each purchaser would also be liable for his pro rata portion per unit of a loan of $800,000.00 made by the sublessors on behalf of the program for 'development expenses' of the mine, the loan being due and payable on December 31, 1991, or at the termination of the lease, whichever was sooner. All notes were to carry interest at twelve percent per annum.

32. The purchasers were to receive a Working Interest and Sublease Agreement from Cascade in its capacity as the Joint Venture Operating Managing Agent for the Joint Venture Partners/ sublessors, who were The Telegraph Mine Limited and Rex Montis acting in its own behalf and as general partner of Gold Technics, Ltd. The operating manager, Cascade, was to receive a one-time initial fee of $800.00 per unit ($28,000.00) for legal, accounting and other services for the year ending December 31, 1980, and

additional compensation of two percent of the actual pre-production (development) expenses, as a development/construction management fee.

33. The terms of the offering as specifically set out later in the Confidential Memorandum and as explained in more detail hereafter, were generally in harmony with the summary. It was particularly stated that the Working Interest Agreement and Sublease required a royalty payment by all of the Associates of twenty-six percent of the gross sales price from the ore mined and sold in each calendar year, or an annual minimum royalty of $2,600,000.00 per year, whichever was greater, following 1980 and 1981 for which special provision was made. It was further stated that beginning with the execution of the Working Interest Agreement and until the time when the recourse notes were paid in full, they were to be paid at the rate of $13.44 per ton of ore mined and milled, and in any event no later than the earlier of December 31, 1991, or the termination of the lease. It was stated that the Operating Manager intended to use the 'shrinkage stoping' method of mining; that it was the intention of the sublessors to build a mill on or near the site of the mine and in the event the mill should not be constructed or proved inefficient, to use established mills in adjacent areas.

II-C. Contractual Control of the Venture by Investors

34. With specific reference to control of the mining operations, the Confidential Memorandum contained various statements. The summary sheet referred to the right of each purchaser of the Units of Working Interests toinstruct the operating manager as to the marketing, disposition or storage of the minerals. In discussing risk factors of the venture, the Confidential Memorandum emphasized investor control:

> In order for the Purchasers of the working interests to avail themselves of. the election under IRC, S 761 it is essential that the Purchasers of the working interests and the Operating Managers and/or other persons, will, as a group, be classified as a partnership and not as an association taxable as a corporation....If the Program should be treated as a corporation rather than a partnership, the election under IRC, S 761 would not be available, the Program would be required to pay federal income tax on its income, and the deduction and credits resulting from the Program would not be available to the Purchasers of the working interests. Also, the Purchasers would be taxed on any distributions substantially in the manner that corporations and their shareholders are taxed. Accordingly, most of the tax shelter benefits would be lost to the Purchasers....

Under Risk Factors it was stated:

> Units in the program are being offered to prospective Purchasers (Sublessees) pursuant to Rule 146 (the 'safe harbor' for private offering exemptions from registration) promulgated under the Securities [sic] of 1933, as amended .. [and that] [i]f a number of Sublessees were to successfully seek rescission, the Sublessees and the Operating Manager would face severe financial demands which could adversely affect their commitment to the Program, and, thus, the non-rescinding sublessors.

35. In the discussion of tax implications the Confidential Memorandum stated:

Centralized Management
Reg. Sec.301.7701-2(c)(3) provides:

> "Centralized management means a concentration of continuing exclusive authority to make independent business decisions on behalf of the organization which do not require ratification by members of such organization. Thus, there is not centralized management when the centralized authority is merely to perform ministerial acts as an agent at the direction of a principal."

Under the terms of the Joint Operating Agreement, the Operating Manager will carry out the ministerial duties required in connection with the operation of the working interests, including maintenance of books and records and preparation of and filing of reports and tax returns. The Operating Manager will not be entitled to make any major decisions concerning the working interests, to borrow money or execute notes binding the Purchasers, to contract for the sale of minerals of a Purchaser without the request of the Purchaser, or make any management decisions or any expenditures outside the ordinary course of business until after consultation with the Purchasers. All major decisions must be approved by ratification of Purchasers owning more than one-half of the Working Interests. Since the Operating Manager's duties are primarily ministerial in nature, and they cannot make any independent business decisions on behalf of the purchasers without their ratification, it would appear that the Program does not have the corporate characteristics of "centralization of management."

Without reference to the tax problem, but in generally describing the Joint Operating Agreement, in harmony with its terms, the Confidential Memorandum summarized the "authority of operating manager" as follows:

> The Operating Manager has limited authority to conduct the day-to-day operations in connection with the mining of the property on behalf of the Purchasers. These acts include overseeing the maintenance and day-to-day operations, the execution on behalf of the program of mining contracts in accordance with the financial projections, overseeing the operations and performance of the Sublessors and contract miners, requiring contract miners to carry sufficient workmen's compensation insurance and public liability insurance and providing the necessary reports and filing to comply with laws applicable to leasing and operation of mineral properties, collect and receive the proceeds from the disposition of the minerals, paying all royalties, costs, taxes and expenses of the operation, causing the proceeds of the Development Loan to be used for the development costs only and providing for the repayment of such Loan and maintaining funds received in connection with the Working Interests not distributed to the Purchasers in a segregated account.

Then, indicating that there could be even greater control by the investors during production, it was stated that the operating manager "will perform the work described in the Agreement to develop the mine to the point that it may be placed into production." The operating agreement itself expressly provided among other things:

operating manager "will perform the work described in theAgreement to develop the mine to the point that it may beplaced into production." The operating agreement itself expressly provided mong other things:

> 15. Actions by the Purchasers. Purchasers owning a majority of Units shall have the power (i) to direct the Operating Manager as to the conduct of the business oftheir working interests (ii) to adjust and pass on the Operating Manager's Accounting, and (iii) to authorize and direct the Operating Manager in management decisions. Anything herein to the contrary notwithstanding, no Purchaser shall have any right to encumber or dispose of any other Purchaser's interest in the property of pro rata share of the ore mined, milled and removed from the Property.

II-D. Personal Liability of Associates for Assessments

36. The Confidential Memorandum in harmony with the copies of basic agreements annexed thereto stated with respect to the "Liabilities of Purchasers":

> Purchasers will be generally liable for their ratable portions of certain losses of the Program in excess of their investment, including liabilities and damages arising out of operating hazards which are uninsured or exceed policy limits because of the joint and several liability imposed by law upon owners of undivided interests in mineral properties (see 'Risk Factors'). The Operating Manager eitherdirectly or through the subcontractors will obtain liability insurance covering each of the Purchasers as well as to meet any requirements under the Lease to the Sublessor. In addition, a Pur-

> chaser will have certain liabilities pursuant to the Royalty Note and the Development Loan....

The first-mentioned liabilities obviously relate not to general operating expenses nor to contracted payments but to uninsured risks assumed by operation of law, in counter-distinction to the Development and Royalty note obligations on which the Associates were liable. Possibility of the insufficiency of the $800,000.00 development fund is tied not to any personal liability but to payment out of production :

> While the Operating Manager believes that $800,000 is the maximum which will be required to expend for the initial development work to get the property into production, there can be no assurance that additional funds will not be required. In such event, it is expected that the funds would be available from production as the development work proceeds.

In negation of any inference that such excess costs might involve personal liability on the part of the purchasers, the Confidential Memorandum repeatedly refers thereafter to personal liability as being limited to the notes, except to the extent that payments would be made out of production assignable to them. On page 23 of the Confidential Memorandum it was stated:

> Although each Purchaser will have no personal liability under the terms of the Working Interest Agreement, except for the recourse Royalty Note, and the development Loan, each Purchaser should be aware of the fact that the working interests are not limited partnership interests in the property. As the owners of working interests, each Purchaser

> is subject to unlimited liability over and above his investment for matters which might occur as a result of the activities, including operations under the Joint Operating Agreement. In organizing TELEGRAPH MINING ASSOCIATES, an attempt has been made to limit the contractual personal liability of the Purchasers. Therefore, the Joint Operating Agreement provides that the Operating Manager, on behalf of the Purchasers, will or cause subcontractors to obtain workmen's compensation and public liability insurance to cover the Purchasers for insurable risks. No provisions have been made to cover uninsurable risks or risks arising out of statutes or regulations by governmental authorities or bodies.

In paragraph 10 of the Joint Operating Agreement, the provisions for "compensation in full for all services rendered" by the operating manager were reiterated, prefaced by a provision for "[r]eimbursement of its out-of-pocket costs of management incurred for the Program which shall include travel expenses and fair allocation or pro rata share of operating, handling, managing and overhead expenses, including expenses for group insurance, safety, hospitalization and retirement, but excluding expenses for any profit sharing payment." In paragraph 13 of that agreement under the heading, Liability of Purchasers, it is stated:

> (a) The liability of the Purchasers shall be severable, not joint or collective. Each Purchaser shall be responsible only for his obligation as herein set forth, and only for his proportionate share of expenses and obligations in connection with the Property.
>
> (b) All costs and liabilities incurred in the exploration and development of the Property and the mining, milling and removal of ore therefrom

shall be borne and paid for by the Purchasers in proportion to their interests.

(c) Notwithstanding anything to the contrary contained herein, the Operating Manager shall have no authority, express or implied, to enter into any commitment or obligation on behalf of the Purchasers or otherwise do anything which would subject the Purchasers or any of them, to any liability in excess of the Purchasers' respective interests in the minerals mined, milled and removed from the Property and their interest in any proceeds from the sale of said minerals.

37. There was no suggestion to the contrary among the "Risk Factors" spelled out in detail in the Confidential Memorandum.

II-E. Risk Factors Reviewed in Contract

38. The Confidential Memorandum expressly pointed out that the investment in the purchase of units -involves a high degree of risk and is suitable only for those persons who have a substantial net worth, no need for liquidity in connection with, and can bear the risk of such an investment including a total loss.' The general risks of such a venture were delineated, as were particular risks relating to mining reserves, the market price of gold and silver, contract mining, labor disruptions in the mining industry, government regulations, weather interruptions, operating hazards, transportation and milling, the unlimited personal liability of the purchasers for the development and royalty notes and on uninsurable risks of the operation, conflicts of interest with particular reference to the various other activities of Rex Montis and the operating manager, tax risks, the categorization as a partnership for income tax purposes, personal liability upon default of notes, risks pertaining to

exclusion from requirements of the Securities Acts, legal counsel, and the complex rules and issues involved in determining the availability to the purchasers of the tax deductions intended to be claimed by them. Among other things it was stated:

> market prices of gold and silver are subject to wide fluctuations....During the period since gold has been permitted to trade freely in the United States, the price of gold and silver per ounce has ranged from a low of approximately $102 and $3.80, respectively, to a high of approximately $875 and $19.25 per ounce, respectively.

The assumption included in the projections was the price of gold for 1981 of $525 per ounce. The actual low for 1980 had been $462 and the high $875. By September 1981 the price had dropped as low as $425; in 1982 it varied between $300 and $500; at the end of 1983 it had fallen to about $350, and at the present it is approximately $325, according to market data of which the Court takes judicial notice. Weston testified at the trial that the price of gold at the time the Confidential Memorandum was prepared was about $600 per ounce and that it dropped to $500 in 1981 and to $300 in 1982. Hodowski testified that he discussed the risks pointed out in the Confidential Memorandum with his advisors and they and he thought the risks were acceptable, considering that the price of gold was about $800 an ounce and there was a possibility of it going up to $2000.

II-F. The Sale of the Offering

39. Prefacing the offering in the Confidential Memorandum was this statement:

The offering for TELEGRAPH Mining AS-

> SOCIATES (The "Program") described in this Confidential Memorandum (the "Memorandum") consists of 35 Units of Working Interests (the "Units"), each requiring an Annual Minimum Royalty of $74,285 per year per Unit. The Working lnterests are for the right to extract gold, silver and other minerals from certain mining claims located in San Bernardino County, California, as more fully described herein. The offering is only available to certain qualified individuals (the "Purchaser") as more fully set forth under "Terms of Offering - Suitability Requirements for lnvestors", herein.

Among other things, it was stated under the heading "Terms of the Offering":

> Each offeree before receiving this Memorandum must complete an Offeree Questionnaire and, where applicable, an Offeree Representative Questionnaire. No offer will be made nor a subscription accepted from a Proposed Purchaser unless such person has the requisite knowledge and experience or unless such person has the benefit of the advice of a representative having such knowledge and experience and such Purchaser demonstrates that he is able to bear the economic risk of the investment.

40. The following is a list of the purchasers of sublease and working interest units or portions thereof in the Telegraph Mine along with their respective interests, as of December 31, 1980, when the offering became fully subscribed:

> Lionel Ascher, Long Beach, CA - 1/2 unit
> Delford R. Ashley, La Mirada, CA - 1 unit

Yukio Ayabe, Honolulu, HI - 1 unit
Jeffery G. Banks, Oakland, CA -1 unit
Phillip M. Bentz, Marina Del Rey, CA - 1 1/2 units
Ronald L. Benzer, Grover City, CA (Benzer Rof foni Partnership) - 1/2 unit
Joseph Bogan, Los Angeles, CA - 1 unit
Coastal Computers Investments, San Luis Obispo, CA composed of Ron Santore, Larry Soderberg and Dale Ouimette) - 1 unit
Elmer J. Davis, Downey, CA - 1 unit
Robert Doub, Whittier, CA - 1 unit
Harry E. Fisher, San Luis Obispo, CA - 1 unit
Jerre M. Freeman, Memphis, TN - 1 unit
Ken Glick, Shell Beach, CA - 1 unit
Joseph Green, Honolulu, HI (Green Higashi Partnership) 1/2 unit
Brent S. Halverson, Alamo, CA - 1/2 unit
Sam and Alyce Hambarian, Orange, CA - 1 unit
Marian Harada, Wahiawa, HI - 1 unit
Harmatz and Hodowski, Los Angeles, CA (composed of Samuel Harmatz and Bernard Hodowski) - 1 unit
David G. Henry, Seal Beach, CA - 1 unit
Charles Y. Higashi, Honolulu, HI (Green Higashi Partnership) - 1/2 unit
Gnolaum Unitrust, Salt Lake City, UT - 1 unit
C. K. Jorgensen, San Luis Obispo, CA - 1 unit
Level II Corp. - 1 unit
Harold H. Masunaga, Wahiawa, HI - 1 unit
C. B. McDonald, Pineilas Park, FL -1 unit
Richard McKean, Salt Lake City, UT - 1 unit
L. E. Muller, Germantown, TN - 1 unit
Robert A. Nickerson, Pacific Palasades, CA - 1 unit
William Y. Ohara, Waipahu, Hl - 1 unit
John Roffoni, Santa Maria, CA (Benzer Roffoni Partnership) - 1/2 unit
Peter P. Samarin, La Habra, CA - 1 unit
George and Patricia Slater, Walnut Creek, CA -1/2

unit
Lowell R. Smith, Salt Lake City, UT - 1 unit
Edwin and Patricia Stoltenberg, Evergreen, CO - 1/2 unit
Herbert W. Stoltenberg, Los Alamitos, CA - 1 1/2 units
Chris Waugh, Long Beach, CA - 1/2 unit
C. T. Whitney, Buellton, CA - 1 unit

Some of the above-listed Associates defaulted early on their obligations as sublessees and their interests were acquired by others. Other individuals, including Roger A. Mann, Kenneth Caldwell (Mann Caldwell Partnership) and H. E. Moses who are defendants and cross-claimants in this suit, subsequently purchased interests. Other Associates have disassociated themselves with the party defendants here, support the good faith and position of Weston, have not been named defendants by Weston and have declined to join the defendants in this suit.

41. Offers and sales of the sublease and working interest units in the Telegraph Mine were accomplished in various ways and by several persons. Weston and Ronald Benzer, an employee of Cascade, attended a conference of the National Committee for Monetary Reform held in New Orleans, Louisiana, in November 1980. They set up a booth in the exhibit section of the conference which displayed materials relating to the Rex Montis mine and Cascade. While Benzer testified at trial that interests in the Telegraph Mine were promoted directly from the booth over a period of two days to numerous people and that copies of the Confidential Memorandum and other Telegraph Mining Associates' offering documents were available at the booth, the more credible evidence indicates that individuals who visited the booth were screened as possible investors in the Telegraph Mine, and if they appeared to be interested in

such a program, they were invited to meet privately with Mr. Weston so it could be determined whether or not they met the suitability requirements and could receive the offering documents. Only two sales of Telegraph Mine sublease and working interests were made as a result of contacts made at this conference. Subsequent to the New Orleans conference, Weston and Benzer, both shareholders in Rex Montis, attended a Rex Montis shareholders' meeting in Honolulu, Hawaii, where Weston explained the Telegraph Mine Associates' offering to a substantial number of attendees at the meeting. Hodowski who was present at the meeting estimated the number at 100; Weston at 20. Also, while in Hawaii, Weston and Benzer met privately with one or more individuals regarding the offering. Six Hawaii residents purchased interests in the Telegraph Mining Associates' offering. On December 2, 1980, a meeting was held in Buena Park, California, which was attended by Herbert Stoltenberg, Robert Doub, David Henry, Chris Waugh, and H. E. Moses, who eventually bought interests in the Telegraph Mining Associates; and also by a number of other persons. As an indication of the difficulty of evaluating broad claims with respect to indiscriminate offerings, Waugh who was present testified that he didn't remember how many persons were actually present at this meeting but inferred that there were many, since the conference room was set up with chairs for forty or fifty persons, whereas Mr. Stoltenberg testified that about fifteen people were present, and it was stipulated at the trial that other Associates if called would have testified essentially in accordance with Stoltenberg's testimony. In addition, Weston went to Oakland, California, to present the offering to Jeffery Banks. Harmatz and Hodowski discussed the offering with several of their clients individually, including Ascher, Davis, Bogen, Henry, Doub, and the Hambarians, and recommended that they invest. Benzer sold interests in the

Telegraph Mining Associates to Rofoni, Fisher, Glick, and Coastal Computers. Brent Halverson advised Caldwell, Mann and the Slaters to invest in the project. Joseph Green referred to Weston five persons who eventually became Associates

II-G. Development of the Mine and Intervention of Investors' Management Committee

42. Not long after the offering became fully subscribed, Weston began to explore the possibility of conducting heap leaching and surface mining at the mine, methods which were not described in the Confidential Memorandum. Over the next several months, metallurgical tests were done to determine the feasibility of heap leaching the ore at the mine and surface mining equipment was acquired. A meeting of the Associates was held in Las Vegas on July 31 and August 1, 1981, at which Cascade presented a proposal to institute a heap leaching operation. The Associates were told that surface mining of certain ore would be quicker and less expensive than the stope and milling method described in the Confidential Memorandum and thus the "scalping" of early profits would be made possible. A vote was taken at the meeting for approval of the proposed heap leaching operation at the mine, and a majority of those present approved the heap leaching plan.

43. Attending the July 31 Associates' meeting in Las Vegas was Mr. Leon Hansen, a consulting geologist who had previously been retained by Mr. Halverson, a CPA who was an Associate and co-promoter of the offering, to visit the Telegraph Mine and report on his observations. On August 6, 1981, Mr. Hansen wrote a letter to Mr. Halverson summarizing his observations and impressions and making certain recommendations of preliminary "staging" activities that he thought should be reconsidered. He expressed the

opinion that the "housing, milling and other rather heavy up-front expenditures are premature and would be considered by many as "promotional in concept" at that time.

44. Subsequently, on August 21, 1981, Hansen and Halverson met with Weston at the Cascade offices in Salt Lake City, and on August 27, 1981, Hansen again wrote to Halverson, this time stating that after meeting with Weston, he felt that there "may be some urgency to consider restaging the program." Hansen indicated that apparently management did not have a "clear picture" of the property situation, i.e., there was some doubt about whether claims had been staked on certain property adjacent to the mine which appeared to be ore-bearing. He reiterated his recommendations of August 6, and also suggested some drastic "restaging" at the mine, including removal of equipment and buildings from the site, curtailing of all utilities at the mine and discontinuance of surface scraping and activity so that further geological and geochemical activities could be conducted "au natural."

45. Halverson wrote a "Memorandum of Concern" to the investors in the Telegraph Mining Associates on September 4, 1981. This memorandum informed the Associates that Weston and Hansen were strongly divergent in their views as to the order of priorities in committing and expending capital on the project. Halverson stated: "Their divergences of opinion with regard to labor, equipment, housing, "home office burden' shared expenses, mining procedural plans, are gross." He pointed out that the venture was highly structured for tax write off, and expressed his opinion that if the economics of the project failed, the tax strategy would also. The memorandum indicated that Halverson and Hansen had suggested to Weston that the Associates might want to defer tax benefits until some "hard core analysis and evaluation of the geologic economic potential of the claims" could be done. Weston rejected this

on grounds that he had to spend capital as outlined in and within the time frame of the Joint Operating Agreement and, in addition, further geological study would be too expensive and the time delay would destroy the tax deductions. Halverson suggested to the Associates a brief moratorium on any further development until a majority of interests could be represented in a meeting with management. It was proposed that local representatives be chosen by the Associates so that a majority in interest of four or five people could quickly be formed through the use of proxies or powers of attorney.

46. On or about September 15, 1981, Benzer, an Associate and the then Vice President of Cascade, telephoned one or more other Associates to express his concerns over alleged improprieties of Cascade and/or Weston with regard to management of the Telegraph Mine. Among other things he asserted:

(a) Certain appendices to the Tomo Ito report which showed very low assay values at the mine, were omitted from the Confidential Memorandum.

(b) Weston's estimates of ore at the mine were highly inflated.

(c) Weston had used a certificate of deposit belonging to the Associates to secure a personal loan to Weston for the benefit of Interphase.

(d) Weston had "padded" the prices, by $1,500 each, of five trailers sold to the Associates by Cascade.

(e) The Associates had been charged excessive amounts for items such as installation of security fence and an archeology study conducted by Benzer at the mine.

(f) Tomo Ito owned an interest in the Telegraph Mine when he wrote his report on the mine.

47. Benzer had obtained a sworn affidavit from Calvin L. Griffiths, an internal accountant for the Associates and Cascade, which tended to support Benzer's allegations of

some financial misconduct on the part of Weston and Cascade.

48. As a result of the various allegations made regarding mismanagement of the Telegraph Mine, a majority of the Associates executed powers of attorney to Herbert Stoltenberg and Chris Waugh to act as attorneys in fact for purposes of investigating the operations at the Telegraph Mine and for removing the operating manager and appointing a new manager if deemed necessary. Stoltenberg, Waugh and Hodowski traveled to Salt Lake City to meet with Weston regarding these matters and with the intention of firing Cascade as operating manager of the mine should the charges prove true.

49. After meeting with Weston for several hours on September 24, 1981, those holding the powers of attorney, denoted "Telegraph Mine Management Committee," became convinced that the mine was being managed properly and that Cascade should stay on as operating manager, subject to the Committee's further conference with Ron Benzer and contact with Tomo Ito. Weston's explanations of t.he major charges against him had been that:

(a) The appendices to the Tomo Ito report were left out of the Confidential Memorandum inadvertently. They had been turned over to Joseph Owens as part of the Ito report when he was compiling his own report on the mine, and had not been returned to Cascade with the rest of the report. This was not known at the time of printing of the Confidential Memorandum.

(b) The estimates of the amount and quality of ore at the mine were not highly inflated. Both Tomo Ito and Joseph Owens determined that there were 72,000 tons of proven ore at the Telegraph Mine and 540,000 tons of probable reserves at the mine. This was considered to be a conservative estimate of the actual ore at the mine. Also, as explained in the Tomo Ito report, although there were

some very low assays at the mine, these were not reliable measure of the average grade of ore at the mine because these particular samples were of the type of ore that shattered and turned to fine-grained material when drilled; thus, much of the gold content would be lost during drilling.

(c) Weston had improperly pledged a certificate of deposit belonging to the Associates as collateral on a loan to Interphase for which he apologized.

(d) The $1,500 added to the price of each of the five trailers sold to the Associates by Cascade was the result of a misunderstanding between Weston and Griffiths, the accountant. Weston stated that he told Griffiths to add $1,500 total to the price of the five trailers, for improvements made to the trailers by Cascade and for transportation to the mine site, and Griffiths thought he meant to add $1,500 to the price of each trailer.

(e) The charge to the Associates for the security fence was fair considering that it encompassed many items such as leveling the land, road improvement, etc., and considering that it was an eight-foot high, chain-link fence surrounding a thirty-acre mill site.

50. While at the Cascade offices, the committee also met privately with Griffiths, who by this time had executed a second, more detailed affidavit which tended to support Weston's explanations of the alleged financial misconduct. In any event, it was agreed upon by Weston and the committee that Weston would henceforth submit budget requests to the committee for approval and checks from the development loan account would be issued or countersigned by a committee member for the approved amounts. Benzer resigned his position with Cascade shortly after making the charges of mismanagement against Weston, and upon his departure took without authority from Weston's office carbon column plans in connection with the leaching operations and various personal papers of Weston, for which he was

sued by Weston in connection with a claim for defamation. The suit thereafter was settled and the missing papers returned to Weston with Benzer's apologies.

51. On October 29, 1981, Mr. Stoltenberg wrote to Harry E. Fischer, an Associate, with reference to the September 24, 1981, meeting, among other things stating:

> After Chris Waugh, Bernie Hodowski and I met with Ron Benzer prior to our trip to Salt Lake City, we were all fairly well convinced that there was a very serious question as to whether the grade of the ore at the Telegraph Mine was anywhere near that which was represented by Tomo Ito and Joe Owens in the Memorandum.
>
> We also felt that there was a good possibility that fraud was perpetrated in the selling of the investment units, mainly because the pages containing the assay results of the ore drillings were not included in the Memorandum.
>
> We also believed that Ron had raised some serious questions concerning the handling and spending of the Associates' funds (i.e., of the $800,000.00 loan proceeds).

Mr. Stoltenberg then described his further investigation and the Salt Lake meeting and the impressions obtained at that meeting:

> Having had our previous conceptions concerning the core drilling sample assays seriously eroded, we felt that the case for fraud had all but evaporated, and that we had insufficient expertise with which to weigh the relative merits of Tomo Ito's conclusions as compared to Ron's (or Leon Hansen's) conclusions.

As a result, we felt that it would be imprudent of us to bring the operation to a halt and possibly jeopardize the investments of all of the Associates, including those from which we had no powers of attorney. We attempted to contact both Ron Benzer and Leon Hansen while we were in Salt Lake, but without success. We subsequently met with Tomo Ito and I had a telephone discussion with Leon Hansen. As we discussed Tuesday evening, Tomo Ito stood by his report 100% He stated that he considered the assays of the core drilling samples to be very unreliable, due to the shattering of the ore. He repeated several times that he believed his report to be quite conservative, both in terms of grade and quantity of ore.

He said that he spent considerable time at the property, including time spent there while the core drilling was going on. He said that he did have an ownership interest in the Telegraph Mine.

Based upon my telephone conversations with Leon Hansen, and upon my observations of his statements and activity during the July meeting in Las Vegas and at the property, I have no reason to question Leon's sincerity. He has impressive credentials, and I found him to be a very convincing advocate of his theories and opinions. I must admit that he created a doubt in my mind as to the accuracy of Tomo Ito's conclusions.

Leon's conclusions, as I understand them, are that the property consists of a series of bifurcating (splitting) veins which pinch and swell, and not of a more or less continuous body of ore as Tomo Ito's report suggests. He further believes that most of the high-grade ore "within reasonable sight" (i.e.

shows on the surface) has already been mined; that there may well be other pockets of ore; but that detailed geology would be required to determine the existence of same.

It did seem to me, however, that the fact that Leon did not take any of his own ore samples, and did not spend very much time actually examining the property might be relevant in connection with the accuracy of his conclusions.

Bernie Hodowski said that on the other hand, he had been present at the property when Joe Owens examined the property and took ore samples, and that he observed Joe taking the samples, and label each sample in a separate bag. Bernie said he had personally carried the rather heavy sack of samples collected by Joe.

As stated above, we felt that it would be presumptuous of considering our lack of expertise on the subject, to make any judgments which would affect the considerable investments of many others.

We did feel that it might be helpful to obtain an opinion from another geologist. As we informed you, we told Dave of our concerns, and he immediately retained Dr. Nead [sic] LeRoy Jensen, who teaches at the University of Utah, to examine the property, take ore samples, and write a report. It is my understanding that Dr. Jensen's report should be finished at this writing, and that Dave will send copies of same to all of the Associates forthwith. I hope that the above is helpful in explaining our actions (or non-actions). I also hope that, in the final analysis, we will all have benefited by the

questions raised by Brent Halverson and Ron Benzer.

52. As a result of the September 24, 1981, meeting of the Telegraph Mining Associates, and by agreement of Stoltenberg, Hodowski and Waugh, Dr. Mead L. Jensen, a geologist and geophysicist, was retained by Weston and a "review" was made of the Telegraph Mine on October 7-8, 1981, "to examine the operations, study geological reports written about the property, and collect samples for assay to verify prior assay results." Based on those factors and that examination, Dr. Jensen made a report of his procedures and findings and submitted the following conclusions and recommendations:

1. The Telegraph area is a previous metal mineralized area of viable potential. Gold occurs in shear zones of minable thickness,'tonnage, and concentration to provide an economically successful venture.

2. Mining to a depth of 450' along the known 2000' strike of the Telegraph (Mine) vein provides a total tonnage of 300,000 T before subtracting 75% reduction for dilution and losses during leaching. (Slurry leaching tanks could rise the leaching operation to more than 90% recovery of -40 mesh crushed material).

3. The tenor of gold varies from nil to several ounces. The average according to my preliminary study and Mr. Ito's results is about 0.354 oz/T but, based on many more prior assays gives a value of about 0.5 oz/T.

4. Using the 0.354 oz/T assay, the gross value of ore is 34,785,000 or $154.60/T assuming $400/oz Au and $10/oz Ag. More than 90% of the

value is derived from gold.

5. My estimate of the cost of the operation is comparatively high, $60/T, because of underground selective mining. Nevertheless, a net profit from 300,000 t, diluted by 75% should be about $17,000,000. (Royalties, lease agreements, loans, interest, etc. are not included because such information is not known by me), As there is visible evidence of the Telegraph vein extending to the north, and evidence of persistence of the vein at depths in excess of 450', the net profit could double to $35,000,000.

6. The development of the property for mining, location of the trailer site and facilities, construction of metal building to house equipment and metal precipitation facilities, and the site of the pads meet not only with my approval but also with my praise.

7a. The prime need of the project is a detailed geological mapping of the area. The petrological and hydrothermal alteration features of the area are of primary consideration of the geological mapping.

b. Geophysical studies of this area are of minor needed significance. I.P. (induced polarization) studies would be useless because of the low content of sulfide and precious metals. Similar objections pertain to electromagnetic (vertical or horizontal and phase shift) techniques. Magnetic studies might aid in identifying varying intrusive rocks, especially alaskites versus granodiorites. But such information would not be too significant, and petrographic studies included in the geological study could provide better results.

c. Soil and rock samples for geochemical prospecting studies are being collected as an ongoing program. I would, however, not recommend any increase over the present program level.

Geochemical prospecting is no panacea for mineral exploration nor does it even seem terribly worthwhile in an area, such as the Telegraph District, where veins are fairly well exposed at the surface. Where the surface indications are not the best, bull-dozer cuts across the vein structure can provide better access for considerably more information than geochemical samples. The fact that Donald Foster Hewett, who I knew, and the author of Prof. Paper 275, located more than 20 veins in the Telegraph area, in the 1920's, by pure geological mapping, and rapid reconnaissance mapping, is indicative of the value of the geological mapping program.

53. Cascade endeavored to work closely with the Associates; committee following their appointment on September 24, 1981, although it proved difficult to coordinate views and activities because of limited communication, day by day problems impossible to solve by correspondence, Weston's desire to operate the mine essentially in accordance with his own ideas and the committee's desire to control expenses essentially in accordance with its own ideas. Each month Cascade submitted a budget request to the committee for the following month. Upon approval of the budget request, the committee issued checks to Cascade from the segregated development loan fund control account in the amount of the approved request. At the conclusion of each month Cascade submitted to the committee duplicate copies of checks, invoices, intercompany billings, equipment charges, and payroll invoices to support the amounts withdrawn. Production through the crusher commenced the latter part of February of 1982. Inclement winter weather hampered production, but in March the-re was an emplacement of 1,145.5 tons of pretreated ore upon the leach pad. In April 1982 an additional 2500 tons were

being sprinkled. The first shipment of concentrates was made April 19, and in its report to the Associates dated April 20, 1982, Cascade indicated that shipments would continue on a regular basis. Its report of April 20, 1982, stated:.

> Now that production has commenced and with the expenditure of all of the loan funds, our quarterly reporting will take on a new format to reflect the cost of production, continuing exploration and development, and the results thereof. A copy of this format is submitted to you for the first quarter of production in 1982. The cost production for the period shown is the amount which is now in excess of the development loan funds.
>
> The first quarter summary also reflects the necessity of selling such of the production, as it is produced, to meet these ongoing mining costs. To date, these continuing expenses have been met by personal advances made by Cascade and myself. These expenses are an Associate obligation. The quarterly summary, therefore, will reflect tons of ore mined during the quarter and the production expenses in dollars. Based upon the average price of metals for the quarter, all expenses will be reduced, in the summary form, to the value of the metals produced. Thus, the quarterly summary will display the net metals either available for delivery or available for sale for your account, based upon your election. For those who would otherwise desire to pay their production expenses in advance, in cash, the ounces of gold and silver shown under "total expenses", less the 5% management fee, would also be available for distribution. Please review the above carefully along with the enclosed quarterly summary and, if you have fur-

ther questions, please call and discuss them with either myself or members of our staff. Otherwise, you should make your election, in writing, to receive in kind, if you so desire, as soon as possible.

54. On August 14, 1982, at Las Vegas, Nevada, there was a meeting of the Associates designated "Second Annual Telegraph Association Meeting and Convention." At this meeting, Mr. Weston, among other things, stated that he was surprised that some Associates had not expected to receive "the second quarterly billing" for "assessable" expenses. He stated that the quarterly billings were necessary because Cascade had paid the start-up operating expenses at the mine in behalf of the Associates since March and the "Operator must restore its credit base." Griffiths, the Comptroller, reported that loans had been obtained by Cascade and David Weston to provide the working capital in behalf of the Associates for the "start-up operations" of the mine in the amount of $372,000.00. Small souvenir bars of gold from the first production of the mine were displayed to the Associates, thirty-five of these bars having been made and it being indicated that they would be distributed to "each Associate who had paid his second quarterly bi11ing." Mr. Hodowski stated that he,Bentz, Waugh, Dale Ashley and Sam Harmatz had come to Salt Lake as a committee to audit the books and records of the company and were happy to report that they found everything in order and above board. He also stated that it could be of more value to the management if a larger steering committee was designated to consist of from five to seven Associates. Mr. Bentz, Mr. Ashley, Mr. H. Stoltenberg, Mr. Waugh, Mr. Green, Mr. .Smith and Mr. Hodowski were nominated as a steering committee with Mr. Doub and Mr. Harmatz as alternates and it was agreed that the ballots should be sent to all Associates, Mr. Stoltenberg to act as Secretary of the steering committee.

55. On October 8, 1982, Mining Engineer Martin J. Hughes made a report upon his engagement by the Management Committee'to review the start-up; to check all methods and procedures and to recommend any appropriate actions which might result in improvement in results." Among other things he stated:

> Problems have been encountered by the Telegraph Project. They have not been excessive and they are of the normal type. Further and as yet unforeseen difficulties will occur. However, the project, if properly supported, is now at the point of consistent operation and good results.
>
> The Telegraph Mine Project has been started in a very good and effective manner. In the writer's judgment, this particular "startup" would compare very favorably to any similar mine initiation.
>
> It is the writer's understanding that a variable cut off grade based upon the price of gold has been imposed upon the Telegraph mining activity [this was by the Associates' Committee]. This requires the Operator to either waste valuable assets or spend considerable amounts of money to stockpile and conserve them. This type of situation can place an unsupportable burden upon the operation and it can actually result in the financial failure of the project. The present cut off grade should be replaced by a blended ore target grade based on realistic projections of the economics of processing the product.

Mr. Hughes also reported that the assaying should be tightened up and perfected-that the work was being done in a "standard and conservative manner" and that subject to any assay-controlled deficiencies, "the results of this program

are acceptable." This report was received for the limited purpose of showing the state of mind of the parties. The Court has also considered, on issues of fact as well as state of mind, Mining Engineer Daley's report as well as others.

56. During the months of October and November 1982, the Management Committee, pursuant to the provisions of the Joint-Operating Agreement and a "Telegraph Associates Resolution- -Management Committee," assumed general control of the operation of the Telegraph Mine. It issued a series of directives to the operating manager, many of which it attempted to carry out. These included the direction that Cascade proceed to obtain the fabrication and installation of carbon columns for the purposes of heap leach mining; proceed to sample hill number one by drilling sample holes; make such investigation as may be necessary to determine if and why CemCorp's atomic absorption assay results [CemCorp was Cascade's own laboratory] were divergent from those of other recognized laboratories which utilized the fire assay method; in the event the fire assay from Assay Laboratories differs from CemCorp's assays, utilize the fire assay results in determining the minimum standard for ore to be mined or processed; make a proposal for a monetary penalty to be incurred by Cascade for all ore mined and processed below this minimum standard; send weekly operating reports, including weekly income and expense statements to each member of the committee until further determination by the committee; meet with Martin J. Hughes, a consultant retained by the Associate Management committee for the purpose of reviewing the Telegraph Mine operations and making a report of his findings, as well as recommendations for change in such operations, and provide Hughes with any and all data he might request and cooperate with him and permit him to interrogate employees of Cascade; crush no additional ore until the entire present stockpile of the ore has been loaded on the

leach pads; not resume crushing operations until an automatic drive has been installed on the crusher stacking conveyer to assure blending of the ore; utilize a front-end loader to take loads from various parts of the stock-pile in loading front-end trucks, in order to achieve some degree of ore blending; not mine or process any ore containing less than $36.00 of gold per ton; determining the dollar value per ton by assuring a 100% recovery of gold from the ore and by using the average gold price for the preceding month; send out through independent assay laboratory (other than CemCorp) all samples for which CemCorp assays indicate a value of .5 ounces of au per ton or bettter and in any event send one out of each fifty CemCorp assays of ore going into the cement haulage trucks to Assay Laboratories at Salt Lake City, Utah, for a separate fire-assay.

57. On November 12, 1982, six Associates who are not parties to the present action notified the Management Committee that they revoked their powers of attorney and the rights given to the Management Committee to represent them, claimed serious mismanagement on the part of the committee causing damages to the protesting associates and affirmed "our rights in and to the Joint Operating Agreement with the Cascade Energy and Metals Corporation as Operating Manager, and reserve unto ourselves every right and privilege appertaining thereto." The next day Dr. Harold H. Masunaga, another Associate not a party to this action, similarly disclaimed the Management Committee's authority, stating that "your actions are gravely endangering my tax structure."

II-H. Weston's Efforts to Collect "Assessments" from the Associates

In prior sections of these findings the general contractual

background and related developments have been dealt with. But it is now necessary to recur more specifically to the basis and development of the dispute which arose between Cascade and the Associates concerning the former's attempts to assess alleged costs of further development and production, which finally led to the institution of the present action by Cascade and the breakdown of the mining venture.

58. On February 15, 1982, in a report to the Telegraph Mining Associates, Cascade stated that, as evidenced from the financial statement accompanying the report, the "predevelopment loan funds will be used up as scheduled about the same time as we are receiving product from the first 5,000 tons of ore leached at the mine site." While some of the Associates paid their so-called assessments and some refused, the circumstances were such as to leave unclear whether the payments made were on the strength of later reimbursement out of production, as a voluntary contribution to implement production, or as a recognition of personal liability beyond the development costs. I have inferred that the first-mentioned alternative was most probable.

59. On April 15, 1982, Cascade, per Weston, reported to Stoltenberg and Waugh as Telegraph Mining Associates Committee that, as was reported in the "March Reconciliation, the predevelopment loan funds, plus the interest accrued thereon, has now been expended in the work of predevelopment." It was added.: "In March we commenced production with the stockpiling of some 1,500 tons of ore." It was further stated:

> You will note that the statement, as shown for March, terminates the contractual obligation to pay 2% of expenses as a development management fee. The production expense, as shown on the statement for March and amounting to S24,493.99

is being invoiced directly to each of the Associate members (which equates to approximately $700 for the lst quarter on a per unit basis). With the facilities in place, it is anticipated that the sale of metals will commence in April. Until cash flow is able to pay directly the overhead costs and the cost of production, loans have been secured by W. David Weston and Cascade Energy and Metals Corporation, to meet the on going expenses with the understanding that the first proceeds of production will re-pay this production financing.

Each of the Associates [has been given] a notice that unless arrangements are made to pay for the costs of mining and processing, royalty, taxes and such other expenses as are incurred in the operation, the costs of mining will be billed to them directly on a quarterly basis and sufficient ounces of the production necessary to cover these costs will be sold. In the event any of the Associates should fail to make the arrangements necessary to take in kind the remainder, or separately dispose of their prorata share of the minerals produced from the operation, then Cascade would dispose of the same at the best available price, remitting the proceeds from the sale, less the cost of sale, to the Associate member.

Thus, the first mention of assessability for the cost of production was on the theory that if not paid, deficiencies would be taken care of out of the sale of the gold, and during a subsequent meeting when the matter of assessments was mentioned, it was in the context that those who did not pay their assessments could not get their gold.

60. On May 5, 1982, Stoltenberg replied to Cascade's April letter concerning his election as to the distribution in kind or in cash of the proceeds of production:

> ... I hereby elect to receive all of my distributions over and above production expenses, in kind (i-.e. in the form of gold and silver metal). The foregoing election would assume that (except for the $1,400 which was my share of the production costs for the quarter ended March 31, 1982, and which I paid to you in cash on April 2lst) Cascade would sell a sufficient amount of the gold and silver (in the ratio in which the said two metals are produced from the mine) otherwise allocable to my two (2) royalties to the lessor, the management fee, payments on the royalty note(s) and development loan, and the production costs, and such amounts as may be reasonably necessary as reserves for exploration, reclamation, further development of the property,,etc. and that the remaining gold and silver metal will be shipped to me in kind quarterly, or at such more frequent intervals as may be practical.

Stoltenberg and the other Associates not affiliated with Weston understood that any advances they had made or would make by reason of the so-called "assessments" were advances against production and did not represent any costs assessable of right except to be paid out of production.

61. In subsequent quarterly statements during 1982, Cascade claimed against each Associate its "share" of "production cost" assessments. The second quarterly billing listed for each Associate a total per unit of $5,781.39 for "Production Expenses" and $1,846.03 for Exploration and development Expense.

62. Under date of December 1, 1982, Stoltenberg, who by reason of his status as an attorney and a member of the Manage-ment Committee, and his liaison with Mr. Weston, had become the spokesman for the dissenting Associates, wrote to Mr. Weston with reference to the threats of Cas-

cade to begin the suit to collect the "assessments." Among other things he said:

> The threat letter from your attorney (which he apparently sent to other "non-paying" Associates) indicates a further absence of common sense, especially in view of the fact that I told you in the November 22nd telephone conversation (and I assume that Phil Bentz told you previously, since I had given him the same message on November 18th) that Bernie, Chris and I had decided to use our best efforts to obtain payment of the second quarter requests for money, and that preliminary inquiries indicated that most of the Associates would pay.

63. On December 2, 1982, Mr. Stoltenberg wrote Cascade stating among other things:

> Please be advised that your proposed budget for November, 1982, (copy enclosed) is disapproved and that among other reasons, the following items are either not justified or excessive: [approximately $35,000 in expenditures covering metal extraction process, fuel, assaying, insurance, tax, license, overhead, management and secretarial, maintenance equipment and electrolytic refining].

The letter concluded:

> The "Existing Bills" are also unjustified under the agreements, as Cascade had no authority to incur liabilities the value of minerals removed from the property.
>
> You are hereby put on notice that any expenses

> or liabilities incurred by you in excess of those which are payable from minerals removed from the property and sold, have been and will be incurred at your own risk.

Weston testified at the trial that this was the first notice he ever had that his advances of production costs were payable only out of the proceeds of production according to the view of the Associates.

64. On December 10, 1982, Stoltenberg sent a letter to all of the Associates reviewing the situation as it then appeared to him. Among other things he called attention to the statement in the Confidential Memorandum that "the operating Manager has no authority to enter into any commitment or obligation on behalf of the Purchasers or otherwise do anything which would subject the Purchasers, or any of them, to any liability in excess of the Purchaser's respective interests in the minerals mined, milled and removed from the property and the interests in any proceeds from the sale of the said minerals." He stated that "the non-assessable nature of the program has been confirmed by Larry Williams, the attorney who drafted the documents" who stated that he intentionally included the non-assessment provisions for the protection of the Associates, as he had done in other mining venture agreements he had drafted. Stoltenberg stated that after the non-assessment provisions were pointed out to Mr. Weston, he immediately changed his theory of liability to the theory that the Associates knew about the "advances" that Cascade was making and consented to them by failure to object and stated that such a theory ran directly counter to the provisions of paragraph 6 of" the operating agreement which required the Associates' express consent to be bound to repay any advances. He stated that it had been difficult to get any particular information from Mr. Weston in view of his predictions of sig-

nificant daily cash flows which were either in process or certain to occur soon and indicated that the Management Committee on September 13 had given Mr. Weston instructions to stop mining and crushing additional ore until certain events occurred and until later that month he stated Weston had stopped mining and crushing on September 21 "due to lack of funds."

65. Stoltenberg concluded as follows:

> In the case of a non-assessable program that encounters cash problems, logic and reason dictate that the promoter attempt to reach an accommodation with all involved, and if he suggests the payment of substantial additional cash by the investors, then he should be prepared to give substantial concessions, especially if he was responsible for the mismanagement or the miscalculations that created the problem.

Stoltenberg also commented on the possibility that pursuant to the Joint Operating Agreement a part of the Associates might commence their own mining operations on the property if they had "paid their billings" as Mr. Weston had suggested. Stoltenberg said:

> But I do believe that if, at this point, some of the Associates start their own operations, and in doing so, use, any of the facilities or improvements, or commence mining on any part of the property which has been paid for or partially or wholly developed using funds supplied by all of the Associates, then the non-participating Associates may well have the right to either enjoin such operations or to demand their share of any profits derived from such operations.

66. On December 14, 1982, Mr. Weston under the heading "Constancy Amid Change 'An Interpretive Opinion'" submitted presumably to the Associates a fifteen-page memorandum explaining his thesis that "the development and production were two separate and distinct phases with distinct provisions for funding by the Associates" and that "production costs were specifically to be paid by the Associates as has been called for as a reimbursement of the operator's expenses." He stated that the Joint Operating Agreement in effect provided that the purchaser had "unlimited" liability for production expense subject to only two exceptions: (1) the authority of the Associates to discharge Cascade as Manager, and (2) the prohibition in Art. 13(c) of the Joint Operating Agreement against the operating manager's subjecting the Associates 'to any liability in excess of the purchasers respective interests in the minerals mined, milled and removed from the property and their interest in any proceeds from the sale of said minerals." Calling special attention to the foregoing expression "minerals mined, milled and removed" and disregarding the reference to "sale of said minerals" he attempted to make determinative his estimation of the value of ore upon the leach pad which of course had never been "removed from the property," much less milled, so that he could justify his billing the Associates for production expense independent of any realization or assurance of realization from minerals mined, milled and removed from the property and any interest in the sale of such minerals in accordance with other specific provisions of the contract relating thereto.

67. This version, presaged but not delineated by Weston's initial attempted justification for the assessments as simply being for expenses which the Associates would have to pay if they immediately wanted their gold in kind rather than waiting for Cascade to sell it and deduct from the proceeds the cost of production, epitomizes a bald

manipulation unworthy of any manager, much less a fiduciary. Add to this the fact that Weston's play with the terms "development cost," "reproduction cost," and "make ready" production costs in an attempt to show that only the former would be covered by the development loan, leaving the latter to be assessable against the Associates, is belied by his projections in the Confidential Memorandum which show production as paying all types of production costs after expenditure of the development loan, and by the notes to the projections which refer to all types of costs relating to production, including preproduction, get ready production and production costs generally, interchangeably as being covered by the cash flow from sales.

68. Mr. Weston in his memorandum placed the burden upon the Associates to protect themselves from liability by directing the operator to stop mining operations when it was determined that the program was not economically viable. He stated that he had never represented or given to anyone an interpretation other than as he then set forth, "indeed, no one has formally requested an interpretation at any time until the Coastal Computer letter" within the preceding month. He suggested a sort of estoppel by observing that "there can be little doubt that the Associates individually or through their authorized agents were willing participants in permitting the Operator to advance funds and improve their assets without objecting and with full knowledge." And he concluded:

> PREPARATION OF THE CONTRACT AND MEMORANDUM. The memorandum and the contract documents were prepared by me, from examples submitted by Larry Williams (corporate counsel). Substantial alterations were made to the format submitted by Williams. The documents were all rewritten and processed on my word processor. The documents were repeatedly

reviewed, altered, and edited to fit our requirements and contract construction. Thereafter, there was a broad exchange of ideas until the documents were in a form that we approved and that expressed our understandings. The contracts were entered into by and between the Associates and Cascade. We are responsible for the intent and interpretation of our contracts, not Larry Williams, who was hired for his tax opinion and his legal advice in regards to the tax and security applications of the program. In illustration, we obtained from Larry an old suit of clothes which were the wrong style and color and didn't fit. After extensive alteration, redying and styling, the suit assumed a new look in fashion. The old suit merged into the new. In this instance the retailoring and new cut design happened not to be made by an outside tailor, but by the new designer/owner. This is as it should be for the new owner has to wear the suit and is responsible to support its appearance.

69. The issue was more sharply drawn between the variant concepts when Cascade threatened to, and did, file this suit and its November-December 1982 report was made, stating that no new ore had been emplaced upon the leach pad during the preceding two months "due to the lack of operating capital and a cohesive, directed program of support among the Associates." It was stated that operations at the mine were at a subsistence level and current production consisted of operating and maintaining the leaching system, the equipment and property. It was further stated that "encumbrance upon all Associates by those who failed to pay their fair share of the start-up production expenses since March was not resolved by mid-December, pursuant to notice" and that "the Operating Manager in protection of

its rights and in support of its obligations and responsibilities to all Associates, has filed an action (complaint) for recovery of the = amounts due the program." It was further stated:

> The suit claims a breach of the Operating Agreement under Paragraph 10 which provides for the reimbursement of the Operating Manager and the Associate's pro-rata share of all operating and other out-of-pocket costs associated with the mine. The Operating Manager has taken the position that the actions of the defendant Associates in breaching the contract constituted a repudiation of the Operating Agreement in its entirety.

70. Paragraph 10 of the operating agreement to which Cascade made reference as a foundation for this claim to reimbursement for production expenses read in pertinent part:

> 10. Compensation and Expenses of Operating Manager. The purchasers agree that the Operating Manager shall be paid as compensation for his services the sum of the following:
>
> (a) Reimbursement of its out-of-pocket costs of management incurred for the Program which shall include travel expenses and a fair allocation or pro rata share of operating, handling, managing and overhead expenses, including expenses for group insurance, safety, hospitalization and retirement, but excluding expenses for any profit-sharing payments.
>
> (b) As compensation in full for all services rendered, the Operating Manager shall receive an Operating Management fee of five percent (5%) of the gross proceeds of the ore mined and sold, (as that term is defined in section 3 of the Lease)

provided that such amount shall be accrued and become payable to the extent of cash available after payment of other expenses from the mining and milling of said minerals removed from the property.

(c) The Operating Manager shall be entitled to receive out of production a Construction and Pre-Production Development Fee equal to two percent (2%) of all costs incurred in the pre-production development of the Program, to construct and develop the property to the production stage.

(d) At the time each Purchaser executed this Agreement, the Operating Manager shall be paid $800 per Unit for legal, accounting and other services during 1980 in connection with its employment as the Operating Manager; thereafter, it shall charge each of the Purchasers the actual costs incurred for such expenses.

71. Paragraph 13(c) and paragraph 15 of the Joint Operating Agreement provided as follows:

(c) Notwithstanding anything to the contrary contained herein, the Operating Manager shall have no authority, express or implied, to enter into any commitment or obligation on behalf of the Purchasers or otherwise do anything which would subject the Purchasers, or any of them, to any liability in excess of the Purchasers' respective interests in the minerals mined, milled and removed from the Property and their interest in any proceeds from the sale of said minerals.

15. Actions by the Purchasers. Purchasers owning a majority of the Units shall have the power (i) to direct the Operating Manager as to the con-

> duct of the business of their working interests (ii) to adjust and pass on the Operating Manager's accounting, and (iii) to authorize and direct the Operating Manager in management decisions. Anything herein to the contrary notwithstanding, no Purchaser shall have any right to encumber or dispose of any other Purchaser's interest in the property of pro rata share of the ore mined, milled and removed from the Property.

72. On December 17, 1982, this action whereby Cascade sought among other things to compel the Defendant Associates to pay the "assessments" it was claiming and to obtain a declaration of Cascade's rights thereto had been filed. On January 10, 1982, Weston, for Cascade, wrote Mr. Stoltenberg cautioning him against the position that the Telegraph Associates' program was non-assessable. He stated, among other things, that "if personal liability of the participants is limited as it would be under your theory-the Association could possibly flunk the exclusion test where the Association might resemble a corporation," and added:

> If your theory is projected further, do you suggest that the Operating Manager is the party obligated for operating expenses beyond the development funds, since it is now evident that the Joint Venture is not obligated? The Associates must qualify as co-owners, each of whom are independently liable, to not be taxable as a corporation.

III. DISCUSSION, INTERPRETATION AND ULTIMATE FINDINGS ON CONTESTED ISSUES

73. From the evidence received concerning the subject matter and the subsequent relations and activities of the parties, the golem-like creature created by the convoluted contract documents has assumed clearer form. In the light of all of the evidence, including hundreds of other documents, extensive and sometimes sharply conflicting testimony, and reasonable inferences, the facts must be deduced as they bear upon the determinative issues. This is not to say that most of the parties and other witnesses with few exceptions did not generally attempt to tell the truth as they perceived it. But some of them from each side saw the truth primarily in the light of their own self-interest as they testified by hindsight, held within only broad limits by written correspondence and other documents which themselves were sometimes only imperfectly revealing. And there were imponderables which clouded the project from the beginning, some of which were listed as "risk factors" in the Confidential Memorandum. A circumstance of pervasive significance was the unpredictable and fluctuating price of gold, with significant declines from the time of the sale of the lease interests to the present time, upon which the venture so much depended at the beginning and the risk of which all parties assumed.

III. Profits from the Associates' Investments did not Depend Solely or Principally upon the Efforts of Others

74. The units sold to the Associates and the investments represented by those units did not depend solely upon the services, actions, or decisions of others for their value but on the contrary the Associates reserved and in actuality

exercised substantial, critical and effective control over the property sold, upon which the value and success of their investments essentially depended in connection with the services of Cascade as joint operating manager. 75. The ultimate right of management and control vested in the Associates by the contract documents is clear and unquestionable as the background review of their provisions has already demonstrated in my opinion. As the previous background findings concerning the control actually exercised by the Associates through their Management Committee has demonstrated, I believe, this right of control was not a mere facade or pretense, but on the contrary was of the very essence of the agreement both in respect to its assumed tax benefits and the ultimate control given to the Associates, a power that was exercised by them to a substantial degree and recognized by all concerned.

76. Herbert Stoltenberg's letter to Harry E. Fisher, dated October 29, 1981, furnishes but one of many examples. He stated that Chris Waugh had attempted to obtain an agreement from Weston for a voluntary turnover to Waugh acting for the Associates of the funds and other assets belonging to the Associates and that Weston had finally agreed. Mr. Stoltenberg wrote: "It was at this point that Chris, Bernie and I flew to Salt Lake City," and he further stated that "in our minds the main purpose of the trip was to take control of the Associates' assets and possibly to terminate Cascade as the operator of the mine (we had received powers of attorney from a majority of the Associates)." Stoltenberg testified at the trial that he believed that they had the authority to take control of the funds of the Associates and terminate the manager. It was only because they became convinced that Weston was acting in good faith and that their monitoring of the funds would serve the purposes of the Associates that Stoltenberg and the others having the power of attorney at that time did not

implement their original intention of taking over the funds and terminating the management upon approval of a majority of the Associates. In 1982, the new Management Committee, as before noted, went beyond the exertion of pressure and monitoring to actively assume direction of operations, and finally to order a shutdown of a part of those operations.

77. In sum, the offering of the promoters did not constitute a security; the investments of the Associates did not constitute securities; the sales to the Associates were not sales of securities within the contemplation either of federal or state laws. Williams in drafting his contributions to the documents initially considered that they were, while endeavoring to emphasize joint control rather than the type of single control inhering in a corporation, together with the controlling rights, and participation of the investors as bearing upon tax benefits. Irrespective of whether he was aiming at an internal contradiction, following the input of Weston and perhaps others, the documents emerged and were marketed clearly as something else, for under them the investors were not relying for their profit solely or essentially upon the efforts of others but upon their own direct and potentially determinative participation in management. In his deposition preceding the trial, Williams expressed some misgivings as to the validity of his initial opinion, but in any event on the basis of the evidence at the trial, I am of the firm opinion, and so find, that at least one essential element of a security, as well as that of the sale of a security, was lacking for reasons above stated.

78. The holding that no security within the contemplation of the federal or state acts was involved renders immaterial the question of whether the offering was a public one or fell within the "safe harbor" or other exemption provisions of those Acts. The evidence as to the latter issues has thrown light upon various remaining material issues in

its suggestion of the circumspection of the parties in limiting sales representatives to the information contained in the Confidential Memorandum, the depth of the participation of some of the Gold Technics Defendants in the selling venture, and the unreliability of some of Benzer's testimony and leaves unanswered why Weston would entrust Benzer in the early stages of the venture with the responsibility he apparently did, and why, if the offering were thought to be a security outside the exemption of any "safe harbor," no claim has been made by the Associate Defendants against any of the Gold Technics Defendants for liability that could arise as a matter of law for failure of registration by them and their joint venturers who made the offering. As to the latter enigma, I have restrained by curiosity, and have struggled first in endeavoring to properly weigh related evidence material to issues in the present case.

III-B. There was no Actionable Fraud or Misrepresentation in the Initial Offering and Sale of the Interests in the Mine

79. The defendants and cross-claimants would have me find that the Confidential Memorandum falsely, willfully and materially represented or omitted facts necessary to render that which was represented not misleading, that is, that the Telegraph Mine claims contained a "highly probable" ore body of approximately 540,000 tons with an average grade of .51 ounces of gold and approximately 2 ounces of silver per ton; that cash flows projected for investors beginning in 1981 and totaling $1,137,339.00 per investment unit by 1991, were based upon tonnage figures and average grades which were erroneous, misleading and overstated on the high side and the operating costs included in the financial projections were severely understated and inadequate to undertake the mining operation described in

the Confidential Memorandum; that David (Weston and Cascade had the experience and ability to place the mining operation described in the Confidential Memorandum into production when in fact Weston had never placed a mine into production; that an underground mining and milling operation would be commenced and placed into production with the $800,000.00 investment loan whereas Weston never intended to commence underground mining as described and knew at the time of the offering that $800,000.00 was insufficient to place the Telegraph Mine into production, and that a representation that federal tax deductions for 1980 equal to approximately 280% of investor cash contributions would be available to each investor was fraudulent. I am urged to further find that there was a fraudulent failure to disclose that Cascade had acquired the Telegraph Mine for $100,000.00, the existence or nature of Weston's previous SEC violations and litigation with other parties, and the appendix to the Tomo Ito report which it is asserted was fraudulently omitted from that report as it was set out in the Confidential Memorandum.

80. Considering the sheer extensiveness of the statements, supporting data and other disclosures contained in the Confidential Memorandum, the exploration of the claims of Benzer and Halverson which were investigated, although largely rejected by the Associates, as early as 1981, the friction renewed as a result of the unauthorized levy of "assessments" against the Associates, the further investigation and the joint management undertaken by the Associates' Committee thereafter with additional access to the details of Cascade's operations, the final opportunity for specification of claims by the Associates long after cooperation efforts had ceased, the heat generated by this litigation, the apparent assumption by the Associate Defendants and cross-claimants that the offering of a security was involved with its further encouragement of multiplying claims, and

the inherent risks of the mining business, including inherent risks of misunderstandings, it is as notable that other charges of misconduct have not been made as that the claims made have been asserted with such convolutions and confusion. They boil down to only few of substance in the context of common law fraud. Most do not warrant extensive comment. Two, relating to the representations concerning ore reserves and the sufficiency of the development fund for the production of ore, are matters of serious concern.

81. The omission from the Confidential Memorandum of mention of the Preston Parkinson v. David Weston and the Gwen P. Weston v. David Weston lawsuits did not constitute a failure to disclose facts necessary to render the other facts disclosed not, misleading. The latter suit was commenced after the sale of the units, the former was filed in October 1969 and settled in 1971, almost nine years prior to the publication of the Confidentiai Memorandum. I precluded retrial of the merits of thislitigation, on the theory that with or without it the outcome would have limited materiality except for needless consumption of time. The alleged failure to disclose securities violation occurring some six years earlier did not constitute a material omission in view of Weston's more meaningful securities problem that was disclosed.

82. The omission of the appendix to the Tomo Ito report was not shown by the evidence to have been intentional; on the contrary, the preponderance of the evidence indicates that such omission was inadvertent, and in view of the indications in the Owens and Tomo Ito reports that the assays in question were not of substantial significance, would have had no bearing or effect upon the investment judgment of the investors who obviously were looking primarily to the text of the Tomo Ito report as confirmed by the Owens report. Hodowski and Waugh had seen the

Tomo Ito report in full prior to its incorporation in the Confidential Memorandum. The absence of the appendix was explained to the general satisfaction of the Associates at the Associates' meeting on September 24, 1981, and the full contents were then available to all interested parties, if not before. It was not until after the present suit was filed that there was any claim by any Associate to a right to rescission of the related contracts on that or any other ground. Far from the disclosure of the missing appendix proving material to his investment judgment, in December 1981 Stoltenberg purchased an additional unit for himself and his brother. The absence from the Confidential Memorandum of the price of $100,000.00 originally paid by Weston for the mining claims was not significant in view of remoteness and the substantial abandonment of the property at a time when gold was controlled at $35.00 per ounce.

83. Neither Weston nor Cascade was shown to have made any false representations concerning their ability or experience or that any such representations should be taken as some guarantee of the success of the venture. There was additional information that could have been given, as revealed at the trial, indicative of their capability and experience which were impressive, and other information that could have been given indicating limitations of experience and ability, which might be true of any prospective manager. A number of purchasers had known Weston for years and observed his capabilities, experience and operations firsthand. Generally, there was a reasonable and fair description of background and experience in the Confidential Memorandum which was essentially factual. Because the mining venture did not turn out as it was hoped it would did not render that which was said insufficient or misleading and did not constitute the breach of any guarantee of success, for, indeed, there was none in this venture of disclosed risks.

84. While in retrospect Weston's projections were overly optimistic and unreasonable, particularly in view of the subsequent change of immediate emphasis to heap leaching operations, the Confidential Memorandum made clear that they were mere theoretical projections on assumptions based upon the geologists' reports and a judgment as to the future price of gold. The proof is insufficient to establish that they were not reasonably believed by Weston to be justifiable projections at the time in light of those assumptions. Among other things, the Confidential Memorandum advised prospective investors:

> Mining Reserves. Although geological reports, surveys and drilling done on the Property indicate the existence of recoverable gold and silver reserves on the Property, there is no assurance that such gold or silver reserves in fact exist to the extent indicated in the financial projections and elsewhere in this memorandum, nor that such reserves are physically or economically recoverable in the quantities indicated.

85. The charge that Weston and Cascade falsely represented the ore content of the mine requires more extensive analysis despite the common law rule that fraud is not to be presumed and it was the burden of the Associates and Gold Technics Defendants, to prove fraud by clear and convincing evidence. It is essential to examine not only the representation on page 9 of the Confidential Memorandum, which is at the heart of the claims of misrepresentation and concealment, but also its context.

86. Immediately above the representation in question, there were summarized figures in the Confidential Memorandum based upon geological reports concerning the "results of the 1969 drilling" north of the number 2 shaft and between shafts 1 plus 2, less dilution factors, totaling

72,000 tons. There is no real question but that this constituted an established body of ore on the basis of the geological reports to which the terms "measured," "proven," or "blocked out," reasonably could have been applied. Then immediately following was the statement at the heart of the dispute as it appears on page 9 of the memorandum:

> In sum, a consultants report indicate [sic] proven and provable reserves of approximately 72,000 tons of minable and merchantable ore including highly probable reserves of 540,000 tons as a part of an additional inferred ore of 1,012,500 tons. (See Geologist Report dated March, 1980, Exhibit G).

87. Attached to and forming a part of the Confidentiai Memorandum was the aforementioned Exhibit G dated March 15, 1980, entitled 'Geologist's Report and Mine Costs Study" by Joseph Owens. Its subject matter was set out under the headings of Summary, Purpose and Scope, Previous Exploration and Reports, Field Work, Location and Accessibility, History and Development, Geology, Mineralogy, Stratigraphic and Structural Control, Grade of Ore, Tonnage Estimates-Measured Ore, Inferred Ore. Illustrations appended to the report were of Major Western Lineaments, Property and Drill Hole Location Map, Topographic Base Map and Plan and Profile. Appended and frequently referred to in the Owens' report were copies of the previous reports of Tomo Ito. The character, qualifications, independence or credibility of Owens and Tomo Ito were not impeached or thrown into substantial question by the evidence, although some of the witnesses for the defendants and cross-claimants at the trial disputed Weston's interpretation of their reports. Owens who testified at the trial was of the present view that there was a

total of 1,012,000 tons of possible ore and that included in that amount were 540,000 tons of probable ore and 72,750 tons of proven ore "that Mr. Tomo Ito came up with." Dr. Jensen was generally of a similar view. Sharply disagreeing, without directly attacking the Tomo Ito report was the testimony of geologist Hansen, called by defendants and cross-claimants, who questioned whether there was any "proven," "measured," or "probable" ore at all at the Telegraph Mine by applying his own peculiar definitions of those terms with little investigation or opportunity for observation and on the basis of his rather arbitrary and unreasoned notions of nomenclature.

88. The Owens' report stated under the heading, Tonnage Estimates-Measured, that "Measured tonnage estimates based on approximately 2000' of OME [Office of Mineral Exploration] drilling were calculated by Tomo Ito and are noted to be extremely conservative." The Owens' report continued: "As reported in 1968 by Ito, two ore zones were blocked out during operations and are reproduced below," the report setting out a table of total "measured" tonnage, less dilution factor and mined stopes, of 72,750 tons with a "[v]alue based on Au, Ag average prices for February 1980 of $26,597,400.00.' Under the heading, Tonnage Estimates-Inferred Ore, the Owens' report stated:

> As indicated by stope sampling, intensity of alteration and open-ended ore zones several reasonable projections of the Telegraph ore Zones can be made. Within the area of the drilling undertaken in 1969 because of the intensity of the alteration and the open-ended ore zones on either side of the drilling and of alteration estimated to extend to depths of at least 450', a proposed ore zone of 540,000 tons i-s expected. With consideration for displacement the gross value of this inferred ore zone would be approximately $146,240,000.

> It also appears reasonable to project because of the open ended ore zones and the strong lineation that is evident between the Telegraph Mine and the Pomona Mine which trends in a north easterly direction and appears to intersect several mines northwest of Interstate Highway I-15, an ore target along the strike of the vein within the present claims as follows: ... Less Dilution Factor 25% =,012,500 tons. Assuming values to existing ore and using March 1980 metal prices 1,012,500 tons at $365.60/ ton = 370,170,000.
>
> This target projection is based on previous stope sampling and on observed intensity of alteration in lower workings. Hydrothermal alteration of this nature is frequently found to be regionalized rather than localized.

89. The Tomo Ito report, a copy of which was attached to the Owens' report as heretofore indicated, was presented under the headings: The Telegraph Mine, History, Principal Features, Mine Workings, and Exposures, General Geology, Mineralization, Tenor of the Ore, Metallurgy and Beneficiation, and Conclusion. The Conclusion of the March 1968 section reads:

> More ore bodies are expected to be encountered, because of: (1) the persistence and strength of the structure (shear zone), (2) the length of the shear zone, (3) the many large quartz outcrops indicating massive vein matter, (4) the many mineralized cross-veins (although small) on the surface, and (5) the relatively small area, even between the two working shafts, which have been explored only to a limited extent.

90. An "Operator's Final Report" was signed by Tomo Ito on April 18, 1969, reporting a drilling program apparently completed by W. S. McGilvray, Jr., and Morgan McGilvray on contract and stating as the basis for the identification of two blocks of ore approximating 72,000 tons:

> The results of the drilling indicates good vein structure to at least a depth of 200 feet on the dip from shaft No. 3 southward to No. 1. For our ultra conservative figuring, orebody is assumed only for 150' to approximately the estimated water table.

The following further observations were made:

> In the drilling process, determination of the vein structure, its thickness, attitude, and composition can be made with a fair degree of accuracy in most types of rocks. However, tenor of ore is most difficult to assess unless in rare cases where the values are evenly distributed in a gangue in which 100% core is available.
>
> Where the values are contained in finely broken and crushed portions of the vein, core recovery is poor and the sludge can be highly diluted. The more shallow holes, such, as 9 and 10, gave evidence of better recovery of values and less dilution of sludge.
>
> Our original plan and projection was based on an average gold content of .50 oz/ton at $35/oz. This conservative figure was adopted after many surface (outcrops, cuts, and holes) and underground (old workings - stopes, etc.) samples were taken and assayed. These results and careful review of

the old records justifies our assumed average value or tenor of ore. To further substantiate our position, a series of samples were taken near the conclusion of our exploratory program, similar to those taken from time to time in the past. This series as shown as Supplement to Appendix A, include samples 2701-2708 inclusive (note: These samples not at expense of OME-costs borne by McGilvrays) excluding 2707. The average gold content of the 7 samples is .51 oz. and the silver is 1.16 oz. On the basis of $40.00 gold ... and $2.00/oz silver, .51 oz/ton is valued at $22.72 per ton. 72,000 tons of ore at this price has value of $1,635,000.

91. Under the heading Observations and Conclusions Tomo Ito further stated in the Operator's Final Report dated April 18, 1969:

> In most cases, drilling results were good, but the writer strongly feels that true information as to values contained is not obtainable in certain types of formation such as encountered at Telegraph. This is especially true when highly fractured vein material with powdered oxides of manganese and iron, together with soft, light carbonates (calcite and siderite) are encountered. This is the type of material most likely to carry high values as shown by sample 2708 (Supplement to Appendix A). Sludge samples submitted where core loss was especially high also may not indicate true values due to heavy dilution. This is particularly true with the deeper holes.
>
> The core drilling program did produce sufficient evidence of vein structure to make it possible to estimate an ore reserve of 72,000 tons of ore. If the ore persists to a depth of 200' on the dip as

indicated by the drill considerable more ore can be added to the reserve. This justifies a beneficiation plant (mill) of modest capacity - 30 to 50 tons. However, such an investment cannot be recommended or even considered until more exploratory work is done.

92. The most difficult problem of intent or scienter is presented by the conflicting testimony concerning "development" versus "production" expense and Weston's at least implied representations that the mine's underground workings could be placed in "initial" production by the expenditure of the development fund represented by the notes of the investors. I have found no direct representation clearly indicating that there might not be additional development expense to be paid out of accruing production profits. On July 28, 1981, in asking for approval of the new surface operations, Weston stated that theearly profits could be "used to suppliment [sic] the pre-development loan funds to assure the continuing full development of the shaft and underground mining operations." He explained, however, that the high interest rates were causing equipment costs to rise appreciably. In this connection it is to be observed that in the mining plan included in the Confidential Memorandum "mining costs" include a listing of equipment in the amount of $919,377.00. There is little to point up any precise amount of development costs in view of other statements in the Confidential Memorandum already referred to and the understanding given to investors that if there were any deficiencies in either the development or production expenses they would be made up by subsequent production, including the revised agreement concerning heap leaching in alteration of the original plan of operation. To add to the uncertainty on this point is the discrepancy between the promoters' belief as expressed in the Confiden-

tial Memorandum concerning the sufficiency of the $800,000.00 development fund for "the initial development work" to get the mine into production and the "knowledge" of Weston prior to December 31, 1980, that the "cost of placing the mine into production would be more than $800,000."

93. On page 12 of the Confidential Memorandum, the following was stated concerning development expenses:

> Development Expenses: Pursuant to the Joint Operating Agreement, the Operating Manager has agreed to perform the task necessary to develop the property, on a best efforts (as more fully set forth in Exhibit D [the Joint Operating Agreement]) to the point of bringing the mining claims into production. The Operating Manager will be compensated for its expenses up to and including the sum of $800,000, as necessary, which sum will include a Construction Management fee of 2% of all amounts so expended.
>
> While the Operating Manager believes that $800,000.00 is the maximum which will be required to expend for the initial development work to get the property into production, there can be no assurance that additional funds will not be required. In such event, it is expected that the funds would be available from production as the development work proceeds.

In their request number 26, the defendants and cross-claimants asked Cascade to admit 'that prior to December 31, 1980, W. David Weston knew the cost of placing the Telegraph Mine into production would be more than $800,000,' and Cascade's response to the request for admission 26 was: "Admit."

94. It is unfortunate that this possible discrepancy was not meaningfully explored by either side during the trial but largely left for exploitation or explanation to the final argument. The context of the admission was not addressed by any offer in evidence of the immediately preceding or following demands and the responses thereto. Weston's counsel in his post-trial brief makes the point that Weston's admission was based on the inclusion of costs for building a mill by the joint venture, not with Associates' funds. The record shows that in addition to the $800,000.00 there was accumulated as interest before full expenditure an additional amount of approximately $75,000.00 which may have been contemplated from the beginning as part of the fund. Nor did any party explore at the trial, or even note in argument, that a belief that $800,000.00 would be sufficient for initial development work to get the mine into production is not necessarily inconsistent with knowledge that to place the mine into production more than $800,000.00 would be required, if the extent of the production was a variable or the source of some of the development cost was to be from early production profits. Weston did testify that the cost of equipment exceeded the amount he had anticipated by fifty percent. He testified he was going to buy for cash or credit. He said the predevelopment loan was "more than enough" to drill 200 plus feet-not 400 plus feet.

95. The Gold Technics Defendants would have me find that Weston individually and through his controlled entities falsely represented to them, both prior to and after the January 1979 and September 1980 agreements, that he and his entities were knowledge- able and experienced in mining exploration, development and production; that the forty-percent interest in the Telegraph Mine to be purchased was not burdened with onerous lease provisions; that Weston and his entities would develop the Telegraph Mine for the benefit of Gold Technics Defendants; that Gold Technics

Defendants would receive their pro rata share of profits, revenues or assets, and that the actual and market value of Rex Montis stock was $2.00 per share. For reasons implicit in what I have already found, and by reason of the failure of the Gold Technics Defendants otherwise to sustain their burdens of proof with regard to these allegations, the Court finds that there were no intentionally false representations of the nature claimed which were relied upon by the Gold Technics Defendants to their detriment, without prejudice, however, to the Court's determination upon a full accounting among the parties whether the Gold Technics Defendants have received their proper share of profits, revenues or assets from the joint venture or their stock ownership in Rex Montis.

96. The investors were told in almost every conceivable way of the legal and practical risks with respect to tax benefit expectations. With reference to the question of the economic viability of the Telegraph Mine in relationship to the Associates' interests, it is significant that most, if not all, of the investors who testified on the point continued to insist that they were maintaining their claim to tax benefits from the project as initially conceived on the theory that the mine contained valuable ore deposits and was economically viable in general agreement with the initial projections. It seems also not without significance that the Gold Technics Defendants are contending in this lawsuit for restitution of their full interest in the mine pursuant to their initial contract for sale of seventy-five percent of their forty-percent interest in the prime lease to Rex Montis. They insist upon their good faith in becoming parties to the venture on the basis of the Tomo Ito and Owens reports on which the Confidential Memorandum was expressly based, but attack Weston's good faith in relying upon those reports without any substantial evidence that he had superior knowledge with respect to their reliability.

97. As to all of these and related matters, the defendants have failed to sustain their burden of proof of establishing that Cascade, Rex Montis or Gold Technics, and those acting with them, did not make their representations in good faith based upon the reports of the geologists, and there is no showing that the geologists whose reports were set out in the Confidential Memorandum did not act in good faith or connived with them concerning, or were parties to any deception. The preponderance of the evidence supports the substantial accuracy of the geologists' reports on the information then available, considering that mineral discovery, evaluation and mining are not exact sciences. That Weston continued to have faith in the program at least into 1982 is indicated by his personal and joint venture contributions after the development fund had been exhausted, by Waugh's testimony that when he asked Weston 'where the ore was," Weston offered to buy him out for $29,000.00 and presented a cashier's check for this amount which Waugh refused because 'it was not enough,' and many other circumstances shown by the evidence.

98. Following submission of the case by the respective parties for decision and the firing of the Court's initial Findings of Fact and Conclusions of Law, counsel for the Defendant Associates has argued that the evidence would at least warrant or require a finding that Weston and Cascade were guilty of "negligent misrepresentation" within the contemplation of California Civil Code S 1572(2). Notwithstanding that the defendants and counterclaimants mentioned that section in their trial brief and in this connection the term 'negligent misrepresentation," the case was tried and argued by them on no such theory, and the issue was not reserved in the pretrial order either as an issue of fact or law. On the contrary, all related issues reserved were based specifically upon claimed securities fraud or common law fraud: "[Contested Issues of Fact[[4]18. Were

the misrepresentations and omissions of fact allegedly made by those identified in paragraph 7 above, intentional and made for the purpose of inducing investors herein to purchase the subject securities?... 19. Were the acts of those identified in paragraph 7 above fraudulent, malicious, or in conscious disregard of the rights of the investors herein?... 29. Did the alleged misrepresentations and nondisclosures allegedly made in connection with the offering violate California Corporation Code Section 25401? [dealing with securities] .... 41. Were misrepresentations and nondisclosures made which violated California and Federal securities laws and who made such representations and nondisclosures? [Contested Issues of Law] [5]13. Have those identified in paragraph 11 above violated California securities laws, including Corporation Code Sections 25110 and 25401?.., 18. Were any of the misrepresentations and/or omissions that were allegedly made by each side material, intentional, and/or fraudulent?"

99. This belated claim of negligent misrepresentations has presented yet another problem difficult for the Court, the evidence having been closed for both sides except as to the accounting and related issues reserved. I have decided, nonetheless, that the defendant and counterclaimant associates have not sustained their burden on any possible issue of negligent misrepresentations both because that issue was not reserved in the pretrial order and was not included in the theory on which liability was tried and because on the basis of the evidence received they failed to sustain their burden of proof by a preponderance of the evidence. Several of the reasons for this are implicit in my findings as originally filed and herein confirmed, and the Court further finds that the representations in the offering were in reasonable reliance upon the geologists' reports to which they were essentially limited, were not established to be materially incorrect, and were accepted and confirmed

by the Associates and their committees after substantially all of the questions as to unreasonable inaccuracy now argued had been raised by Benzer.

100. With reference to the risks of the venture which were outlined in the Confidential Memorandum and assumed by the investors, the Court is mindful of legal and equitable considerations which preclude promoters from insulating themselves from liability for fraudulent misrepresentations by reciting in small print or otherwise risk factors relating to the dangers of the investment. But the good-faith recitation of variables or uncertainties inherent in the nature of an operation may bear upon the question of whether, indeed, there has been a representation to the contrary, the reasonableness of any representation and the intent or lack of intent on the part of the promoters to mislead or deceive and may, depending upon the circumstances, be the badge of fraud, or a badge of fairness andcandor.

101. Weston and Cascade were no doubt guilty of errors of judgment in their initial evaluation of the immediate minability of the underground ore and in the ultimate realizations projected; and in their subsequent claim that the documents of contract provided in effect for assessable personal liability of the Associates for development and their use of a portion of development funds for unauthorized purposes they acted wrongly. But I have concluded that the evidence is insufficient to prove that their initial conduct was with fraudulent intent or scienter. The venturing by Cascade and Weston of their own resources and those of the joint venture without any assurance that they would be reimbursed other than through production is a further indication to the Court of Weston's confidence in the ultimate success of the venture and the good faith of his representations with respect thereto. The whole initial venture simply did not bear the badges of a fraudulent

enterprise at its inception for reasons heretofore indicated. The defendants and counterclaimants having the burden of proof, and securities not being involved, in the absence of preponderating evidence, much less clear, satisfactory or convincing evidence to the contrary, the Court will not presume fraud.

102. In view of failure of the complaining parties to meet their burden of proof with respect to the alleged misrepresentations or concealments charged by them, the Court finds generally, except as otherwise specifically stated, that to the extent they were made or were implicit in the general plan of operation set out in the Confidential Memorandum, no scienter or intention to deceive or mislead existed on the part of Weston and the interests he represented; that there was no negligent misrepresentation; that there was no showing of excusable ignorance of misrepresentations on the part of the investors; that there was no justifiable reliance upon any allegedmisrepresentation, and that any absence of information or material now complained about would not have had significant effect upon the investment judgment of reasonable investors and particularly of the Associates who committed themselves to the venture in good faith knowing of the risks and with the expectation that they might achieve high profits in tax benefits and otherwise or lose their initial investments and tax benefits by reason of those risks.

III-C. The Associates were not Personally Liable for "Assessments' and Plaintiff's Related Complaint Fails

103. Included in the report of Weston to the Telegraph Mining Associates Committee dated April 15, 1982, were thefollowing statements in addition to those quoted in part II indicating that Weston then believed that the hope of placing the mine into profitable production and reimburs-

ing advances made or secured by him and Cascade depended upon substantial additional financing from the Associates which could be induced by holding out prospects of production out of which such advances on the part of them and the Associates might be paid.:

> With the facilities now in place, it is anticipated that the sale of metals will commence in April. Until cash flow is able to pay directly the overhead costs and the cost of production, loans have been secured by W. David Weston and Cascade Energy and Metals Corporation to meet the on going expenses with the understanding that the first proceeds of production will re-pay this production financing.
>
> Each of the Associates, with the last quarters report, are being sent a summary of the pre-development loan fund expenditures to date. In addition, a notice that unless arrangements are made to pay for the costs of mining and processing, royalties, taxes, and such other expenses as are incurred in the operation, the costs of mining will be billed to them directly on a quarterly basis and sufficient ounces of the production necessary to cover these costs will be sold. In the event any of the Associates should fail to make the arrangements necessary to take in kind the remainder, or separately dispose of their prorata share of the minerals produced from the operation, then Cascade would dispose of the same at the best available price, remitting the proceeds from the sale, less the cost of sale, to the Associate member.

104. It is my opinion that despite other complications in the documents purporting to govern relationship of the parties and their responsibilities and liabilities toward each

other, there was no lack of an initial understanding among them, including Weston, that once the mine was in production it would produce sufficient cash flow to assure not only the production costs but profit for the parties in accordance with the projections. This is the only explanation the Court can find for absence in the contract documents of any means or mechanism for paying production costs except out of the realizations from production, indeed, for their negating any personal responsibility for such payments on the part of the Associates except out of the proceeds of production and with the inherent rectifier of putting it within the power of both the manager and the Associates as such to bring operations to a close when not sufficiently successful to provide for a profit above expenses.

105. And one of the important indications to the Court of Weston's good faith in the beginning is the very absence of such provisions and his subsequent willingness to commit his credit and that of interests he controlled to raise funds to keep the operation going without any real assurance of any reimbursement except from production. But I find that there came a time when his confidence turned from profits from production to unjustified insistence that the Associates subsidize Cascade operations and advances independently of any expectation of reimbursement from production.

106. The Court finds that the Telegraph Associates were obligated and liable under the Joint Operating Agreement and sublease only for the minimum annual royalties and their pro rata share of the $800,000.00 predevelopment loan and had no contracted to be liable for the personal assessments which Cascade sought to collect beyond and aside from profits from production. Cascade and Weston on their own or for the joint venture incurred additional operating expenses for which they now seek reimbursement through 'assessments' but there was no promise or representation

by the Associates that they would pay the operating expenses relied upon by Cascade prior to Cascade's obtaining their loans or incurring the expenses other than from proceeds from the production of gold. The loans obtained by Cascade were voluntary, without express consent, initially without even the knowledge of the Associates and were in justifiable reliance by Weston and Cascade only upon the prospect of obtaining reimbursement from production, aside from the question of responsibility of the joint venture to the extent they represented that venture.

107. Weston testified at the trial that the only way the Associates could have terminated their continuing obligation to pay Cascade's assessments was by default of their royalty obligations or Cascade's discharge as joint operating manager by majority vote of the Associates. Such an interpretation seems especially bizarre and oppressive not because the Associates had no power to discharge the manager or to bring their royalty obligations to an end by default, but because it indicates that Weston sometime in 1982 had developed the idea that without reference to profitable production of the mine Cascade could secure continuing financial advantage through claims to the assessments that he must have then known were not justly due under the agreement except out of production.

108. With this knowledge, payments of assessments were received by Cascade from a minority of Associates who are parties here in varying amounts and the other defendants and counter-claimants failed and refused to pay any of the so-called assessments. Treatment made of the "assessment" payments actually made will be reserved for the accounting hereafter ordered.

III-D. Plaintiff has Shown no Entitlement to Recover on a Quantum Meruit Basis against Defendant Associates

109. The Telegraph Associates were obligated and liable, under the Joint Operating Agreement-and Sublease, solely for the minimum annual royalties and their pro rata share of the $800,000.00 predevelopment loan, and were not contractually liable for any "assessments' as aforesaid. Cascade had effectively expended or transferred the entire $800,000.00 predevelopment loan by the early part of 1982. Cascade and Weston then obtained loans beginning in February 1982 and continuing in March and early April 1982 and did not advise the investors in advance that they would look to the investors to pay the operating expenses or loans if gold production was insufficient to pay them. To the contrary, all of Cascade's communications with the investors advised them in effect that production expenses ultimately would be paid out of production and it was implied that any investor payments would be interim financing or in order that they could receive their corresponding gold production in kind. Cascade on its own incurred operating losses for which it now seeks payment through "assessments." The loans and continuing operations were for Cascade's own expected benefit and/or that of the joint venture. The Joint Operating Agreement specifically provided at paragraph 6 that Cascade was not empowered to modify the agreement or to 'borrow money or execute notes or other instruments of indebtedness binding the Purchasers of said units without the express concurrence of the Purchaser of said units...,' which concurrence was not received. The participation of the Associates' management committees in the expenditure of such funds did not estop

them or, the Associates from contesting their reimbursement because of the frustration by Weston of the purposes and intent of continued operations of the contracts through unjustifiable assertions of liability on the part of the Associates, his holding out prospects of profits out of production which were illusory, and the de facto expiration and termination of the subleases as hereinafter found. Cascade's improper attempt to saddle obligations upon the Associates for which they were not obligated under the circumstances cannot be' implemented by the Court either under theories of quantum meruit, promissory estoppel, unjust enrichment or at all. These findings are qualified by, and without prejudice to, possible liability of Gold Technics Defendants for some of these expenses on the theory of contribution or quantum meruit, to be further considered as a part of the accounting to be ordered in this case.

III-E. No Tort or Negligence Liability between or among the Parties has been Established

110. None of the cross-claimants or defendants was guilty of making false or defamatory statements of or against any other party which were not privileged, nor did any of them tortiously or otherwise interfere with any contract or prospective economic advantage without the privilege so to do under the law and no party herein is shown by the evidence to be entitled to damages for any tort against any other parties or party. The communications and dialogue by the parties concerned with reference to the operation of the mine and of rights or obligations in connection therewith were at times robust, pointed, critical, to an extent speculative or exploratory, and sometimes vituperous, but all of this was within the realm of legality in the Court's

opinion and those claiming damages therefor have failed in their respective burdens of proof.

111. Aside from the question of accounting and any mis allocation of obligations, debits, credits or funds, and aside from the question of whether the conduct of Cascade and Weston frustrated or terminated the sublease and obligations thereunder, the Court cannot find by a preponderance of the evidence that Cascade was guilty of actionable negligence in its services as Joint Operating Manager, particularly as they were monitored, supervised or controlled by committees of the Associates, and thus finds, by reason of failure of proof, that the plaintiff was not negligent and that neither the defendants nor the cross-claimants are entitled to damages for negligence in the operation of the Telegraph Mine.

III-F. Rescission is not Warranted

112. The defendants and cross-claimants have asserted that the Working Interest Agreement and Sublease were breached by Weston and Cascade by proceeding with mining activities without any evidence that there existed minable and merchantable gold and silver and by reason of the failure of the efforts of "an incompetent and inexperienced promoter.' They claim that Cascade and Weston breached the Joint Operating Agreement by operating at a loss and seeking to commit the investors to operating losses far in excess of the investors' interest in the minerals mined, milled and removed from the property and accordingly seek rescission of the contracts ab initio. I have already sufficiently indicated the reasons for believing, and hereby finding, no grounds for such rescission have been established as distinguished from the recognition of termination of the

sub-leases and future obligations thereunder.

113. There are insufficient factual, legal and equitable bases established by those having the burden of proof for rescission of either the sale to the predecessor of Gold Technics of its interest in the Telegraph Mine or the sale by Gold Technics to Rex Montis of a portion of that interest. Neither seller has done or offered to do equity in connection with any such attempted rescission. All claims for rescission and restitution of consideration are inextricably involved in the other issues of this litigation and the incomplete accounting among the parties. Neither seller sought to exercise any right of rescission it may have had within a reasonable time or before it had made irrevocable elections with knowledge of the facts, and both have waived any rights to rescission by delaying its timely assertion and taking action and receiving benefits inconsistent therewith in the meantime. The original claim to recission was outlawed by the California statute of limitations. I am not unmindful of the offer purportedly on behalf of Rex Montis after this litigation commenced to rescind the purchase from Gold Technics and of the purported acceptance by Gold Technics more than a month thereafter. The "offer" was not signed but was transmitted to Harmatz and presumably the other members of Gold Technics by a letter dated January 25, 1983, from an attorney representing Rex Montis; it specified that acceptance had to be within thirty days after receipt. The purported acceptance was mailed by Harmatz to Weston on March 3, 1983, with a notation that it was signed by 'all but two of the partners," (which was a majority authorized to act for the partnership) but was on the express condition that it would cancel the right of Rex Montis to a thirty-percent interest in the Telegraph Mine and with the request that Weston acknowledge forthwith in

writing his agreement with this interpretation (which had been placed in doubt by the letter transmitting the "offer"). No acknowledgement of this condition appears of record. The delay in responding to the purported offer, superimposed upon the prior delays, the failure of Gold Technics to restore or tender the consideration for the original agreement and any benefits received as a result, its unreasonable speculations upon developments at the mine and the changing fortunes of the litigation, and other related circumstances, render the purported offer in course of the litigation little more significant as a waiver than the unconsummated request on purported behalf of the Defendant Associates for an extension of their royalty note "obligations" for force majeure was a bar to my determination that the sublease obligations should be deemed already to have expired. Rex Montis will be deemed to hold the 480,000 shares of stock in trust for Gold Technics, subject to accounting for the initial purchase price of Gold Technics' interest in the mine and the other matters of accounting among the parties hereby reserved.

114. Nor do I believe that Cascade for itself or on behalf of the joint venture is in a position to assert any claimed breach of contract as a basis to rescind the interest of the Defendant Associates in the mine and yet to hold them for unpaid rental or royalty or development note obligations, under the circumstances peculiarly applicable to those Associates and because of application of the doctrine of unclean hands against Weston and Cascade.

II-G. The Subleases of the Mining Claims of the Defendants and Cross-Claimant Associates were Terminated without Obligation on their Part for Further Payments of Rental or the Royalty or Development Notes.

115. The contract documents set out in the Confidential Memorandum and the Joint Venture Agreement were contracts of adhesion, each of which became a part of the offering, all of which were implicated in the relationships, rights and obligations of the parties, and all of which should be interpreted and considered in pari materia. This is especially so because in all of their actions concerning the Telegraph Mine from the inception of the joint venture, Weston and Cascade represented not only themselves but also the joint venture as sublessor.

116. It may be that the venture was destined to fail from the beginning by reason of its complicated structure, its expansive design for tax benefits as well as operating profits, a kind of dichotomy between the interests and powers of the investors and their control for this and other purposes and the centralized services of the operation manager; the conflicts of interest and commingling of interests that had been accepted and approved, the market's failure to sustain the price of gold upon which expectations of the investors were importantly based, the lack of provision for adequate financing of production in its early stages in order to sustain and expand that production until the projection of profits from production better could be realized, and other circumstances not directly related to the intrinsic value of the claims as a mine property or the mis-representations claimed to have been made. But these involved errors of judgment shared by all of the parties in varying degrees and

not fraud. The property does contain extensive deposits of ore that under a different organization, contract, management, royalty, cost or financing structure might have been operated at a profit from the gold and silver produced therefrom during the participation of the Defendant Associates. But in the context of the subsequent developments that have been reviewed above, and in light of principles of equity and good conscience which neither Cascade nor any of the other joint venturers represented by it can question, the very premise and purpose of the contracts, and particularly of the subleases, became impossible to achieve as far as the party Associates were concerned because of Cascade's program for compelled and unjustified subsidization of continued operations at a loss, when use for convenience of the term "party Associates"2 in this and similar connections hereafter is intended to be synonymous with the term "defendant and Gold Technic Associates" used elsewhere and does not include unit owners who are Weston controlled companies. it had become obvious to Weston, Cascade and to the joint venture that no 'minable and merchantable ore'could be produced without financing of early production costs beyond the profits therefrom and the obligations the Associates had contracted and assumed in connection with the purchase of their sublease interests. More particularly Cascade entered into a program of misrepresenting to the Associates its knowledge of this lack of

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2 Use for convenience of the term "party Associates" in this and similar connections hereafter is intended to be synonymous withthe term "defendant and Gold Technic Associates" used elsewhere and does not include unit owners who are Weston controlled companies.

immediate profitability in order to induce or compel the Associates to finance its continued operations without reference thereto, under the guise of a claimed legal obligation on the part of the Associates, continued its unjustifiable demands, brought a wholly unwarranted suit against the party Associates in an attempt to enforce them, terminated the lease interests of the party Associates because of their failure to comply with its unjustified demands, and thus defeated any prospect for working out the problems of financing amicably among the party Associates and the other interests involved to the extent then essential to permit their participation in the production of minable and merchantable gold and silver. In its representation and conduct as Joint Operating Manager for the Associates, including necessarily its inextricable involvement as agent for the joint venture, Cascade occupied a fiduciary position under which it owed utmost good faith and essential candor to the Associates. The burden of proof and presumptions between the parties in such relationship are quite different than they were with respect to any issues of fraudulent or even negligent misrepresentation when the parties were dealing at arms length. The party Associates have sustained their burden of proof to establish that Cascade breached its fiduciary duty toward them in respect to the frustration of the prospect of minability and merchantability of the gold and silver at the Telegraph Mine so far as their interests were and are concerned by its contrived termination of their sublease interests and its antecedents as here in found.

117. Even with the benefit of hindsight, mining people demonstrated at the trial such variant opinions and judgments as to renew and reinforce the experiences of history of which the Court can take judicial notice that mining ventures even when all of those concerned are proceeding in good faith frequently involve unanticipated failures as

well as surprising successes, and that practical development work and actual mining operations teach more surely than theoretical predictions or projections, however reasonable they may have first appeared. Weston following the sale of the subleases undoubtedly acquired extensive information concerning prospects at the mine considerably beyond that which had been provided in the Tomo Ito and Owens reports. He enjoyed from intimate and practical observation a preferred position to reevaluate the practicality of producing minable and merchantable gold and silver from the underground operations and its timing within the structure that had been established and the extent of profits, if any, that might be realized from surface heap leaching. Obviously, at some point Weston had concluded that continued production would depend not upon the profit to be immediately generated therefrom but upon subsidizing by the Associates of the costs of further development and production through "assessments" he at first had hoped would be voluntarily made by them upon their expectation of reimbursement out of production but which he at length considered it necessary to assert as their legal obligation under the Joint Operating Agreement in order to afford any possibility of continuing to operate the mine. In spite of the additional subsidization that Weston and Cascade had arranged on their own credit or that of the joint venture and the additional funds they had induced some of the Associates to contribute beyond their responsibility, Cascade simply could not immediately produce 'minable and merchantable gold and silver." By November 1982, demands for the payment of further assessments not being complied with, Cascade had in effect suspended mining operations and reported to the Associates that the property was, and would continue to be, on a maintenance basis until the Associates complied with its demand for the payment of continuing assessments, virtually holding valuable minerals

Weston claimed to be on the leach pad as hostage for his unjustifiable demands. From that point Cascade's efforts turned from managing the mine within the intendments of the agreement with realistic hope of producing the expense of operation at a profit, to a program simply to compel the Associates to make unwarranted contributions for an indefinite period of time for which they were not bound.

118. Each sublease provided that it would continue in duration "until all minable and merchantable gold and silver has been recovered by Sublessee from the mining claims. "Minable and merchantable gold and silver for the purpose of the sublease and the related contract documents was stated to "mean the gold and silver contained on and under the Mining Claims which, at the time it is reasonably reached in a proper plan of mining and development, can ordinarily be economically mined and marketed by the use of the then modern and efficient equipment, method and adequate management, at a profit by Sublessee." In view of their cutting off the interests of the party Associates as aforesaid and as hereinafter further found, Cascade and the interests it and Weston represented are hardly in a position to say that they did not pursue "a proper plan of mining and development" or did not endeavor to economically mine and market the gold and silver by the use of then modern and efficient equipment methods and adequate management and they cannot deny that the mining was not at a profit to the party Associates and never can be in view of developments following the subleasing and particularly the unwarranted conduct of Cascade. In view of these circumstances the term 'minable and merchantable gold and silver" will be construed liberally in such light in favor of the party Associates against whom Cascade and the joint venture are seeking to enforce claimed liabilities for payment of the royalty and development notes, as well as the "assessments." In equity and good conscience the subleases should

be deemed to have expired as far as the party Associates are continuing liability on the part of the party Associates to make rental and development note payments that have not already been made in cash.

119. A similar result is reached upon the basis of Cascade's own action in subsequently "terminating" the subleases of the Associates who are parties to this suit. On February 3, 1983, on stationery of the "Telegraph Joint Venture" the Telegraph Mine Joint Venture by W. David Weston for the Executive Committee, addressed a letter to each of the party Associates and giving notice of the termination of the subleases, reciting that the Associates appeared to "totally disregard the good-will efforts of the joint venture to assist you in securing a pro-rata recovery of the reported $1,800,000.00 plus value of the precious metals presently under leach" and demanding satisfaction of alleged individual obligation for payment of the "1980 recourse note $44,285.00; 1981 recourse note $44,285.00; development loan $22,857.15." But the specification of defaults went beyond these items and included failure to pay pro rata share of costs incident to "prospecting, engineering, surveying, development and mining of the property" (reciting that production from the property commenced in March of 1982) amounting to $15,419.62. It was stated that "liens have been or are being filed against the property for this amount by the Operating Manager/Contractor in behalf of itself, its sub-contractors and suppliers; failure to pay the sublessor for its services in crushing and hauling ore 'mined in your behalf at the property, in the sum of $6,564.51'; failure to pay during the calendar year 1982 payments on the prior royalty notes at the rate of $13.44 per ton of ore mined, to be paid quarterly until fully paid, all of which payments ... are in arrears amounting to $9,580.17; failure to pay pro rata share of taxes which are in arrears and for which liens have been filed against the property in the sum of $325.00."

I find this notice manipulative and especially egregious in some of its aspects. For example, the claimed tax liens and Cascade's threat of filing a lien on behalf of itself and its subcontractors and suppliers as establishing the Associates' default for permitting a tax lien and other liens to accrue against the property were ironical, even bizarre, in light of the great value of the gold Cascade said was on the leaching pad and Cascade's own duty to use reasonable effort to realize that value to meet any financial obligations of the Associates and for their profit.

120. On or about March 3, 1983, Weston for Cascade and as managing agent of the Telegraph Mine Joint Venture, gave 'notice of forfeiture termination of lease' as of February 3, 1983, to 'Telegraph Mine Sublessees (Associates)." The notice was spread upon the public records of San Bernardino County, California. This termination was unconditional and, however contrived its reasons were, had the effect under the circumstances to confirm the fact that in equity and good conscience the subleases of the party defendants had come to an end, together with any obligations to make payments of their royalty and development notes.

121. The 'Telegraph Mining Associates' Working Interest Agreement and Sublease" was signed separately by each investor. The Sublessor was Cascade "as the managing agent of the Telegraph Mine Joint Venture." All subleases were signed for the Telegraph Mine Joint Venture by 'agent and manager" Weston who was noted as "President (hereunto duly authorized)." The evidence leaves no room for doubt that Weston had full authority by virtue of governing contracts over both the existence and the termination of the party defendants' subleases, subject to termination by their own terms or as matters of law and equity. The Working Interest Agreement and Sublease provides in part as follows:

> 20. Repossession of the Premises. Except as may be otherwise provided for herein, if default be made by Sublessee in the payment of the Royalty or in the performance of any other terms or conditions hereof required to be kept and performed by Sublessee and such default shall continue for a period of one month after written notification thereof to Sublessee, then, in such event, and as often as the same occurs, Sublessor may, at its option, terminate this Sublease and reenter upon and take possession of the Sublessee's interest in the leased gold, silver and other minerals and leased premises and every Part thereof, and be reinstated in its possession to hold as if this Sublease had not been made. Such action by Sublessor shall constitute the Sublessor's sole remedy in the event of default in payment of the rent and shall result in the forfeit of its right to rent due or accrued up to the time of such termination and reentry.

Cascade and the joint venture contend that the forfeiture of their right to rent due or accrued up to the time of such termination did not include the forfeiture of payments by royalty notes already given at the time nor the payment of development notes by the party Associates. Irrespective of whether the last quoted provisions of the agreement technically can be construed favorably to the non-drafters to bar recovery on the royalty notes already delivered, for reasons heretofore stated, I hold that under the doctrine of unclean hands which is a pervasive one and can be applied by a court of equity under appropriate circumstances on its own motion in the public and judicial interests as well as that of aggrieved parties, Cascade and the joint venture should be barred from any remedy against the party Associates for the collection of the royalty notes or development notes ex-

ecuted by them. It may be observed without ascribing determinative force to the provision standing alone and out of the context of the party Associates' situation, that the last quoted provision not only would forfeit "right to rent due or accrued" but provides also that the action of termination shall constitute the sublessors' "sole remedy in the event of defau1t." While the paragraph preceding the one quoted reserves to sub-lessor other remedies available under the laws of the State of California for violation of any covenant or condition, there is added thereto "except as may be otherwise provided herein." It was so otherwise provided. If there were perceived to be any ambiguity in this respect it would have to be resolved against the sublessor since the sublessee had no hand in the drafting of the documents which were the product of Weston and those interested in the joint venture.

122. In any event, it is reasonable and proper under the circumstances to bar Cascade, the joint venture and affiliated interests from recovery against the party Associates of unpaid rental or royalty under the subleases, whether represented by royalty notes or not, and from recovery on the development note. All party Associates are free from any liability for unpaid "assessments," and the Court will consider in the accounting the extent, if any, that assessments already paid should be refunded or applied to expenses incurred by Cascade in connection with its management of the mine with the Associates' committee. Since all of the contract documents set out in the Confidential Memorandum, together with the Joint Venture Agreement, were contracts of adhesion in view of the interlocking agencies, the termination of royalty and development note obligations of the party Associates as to one should have effect of terminating the obligations of the Associates under all, without prejudice to the Montis and Weston in which equities among those parties will be considered.

IV. EQUITABLE REMEDIES AND FURTHER PROCEEDINGS FOR AN ACCOUNTING AND RELATED RELIEF

123. Cascade and Weston were reasonably obligated to render a fair, understandable and reasonable accounting of all funds received, expended or disbursed for or on behalf of the Associates and the Joint Venture. This Cascade and Weston have failed to do for various reasons, including the complexity of the accounts, the confusion of channeling funds through various corporations under the control of Weston, the allocation of funds among accounts as Weston or his bookkeeper Griffiths under his direction may have determined, the crediting, charging and allocation of funds on the theory of the "assessability" of the Associates' interests beyond profits from production, the unqualified claims for liability of the Associates for funds borrowed or contributed by Weston, Cascade or the joint venture for expenses at the mine beyond the development fund and production profits, and other misconceptions and uncertainties concerning the contractual rights and obligations of the Associates. The investors had been fairly advised from the beginning of possible conflicts of interest of Weston's interlocking ownership and activities and were on notice that there would be the interchange of funds among the various entities involved in the ownership, financing and operation of the mine and related entities; this did not obviate the necessity-of full and proper accounting. Cascade as operating manager expressly agreed that it would maintain separate accounts for the operation of the mine and the Associates' interest therein. Even though it were to be assumed that this did not require the establishment of separate bank accounts, and that Weston's general system of Tandy Corp computerized accounting could have been adaptable for the purpose, its actual utilization as thus far

demonstrated at the trial fell far short of reasonable requirements. An accounting has not yet been made in such form and substance as to be suitable for the final accounting of a fiduciary, or the necessity for which was obviated by the monitoring of committees representing the Associates, some of whose members also may have been in conflict of interest positions because of their relationship to the joint venture.

124. Weston generally was able to support his accounting system and to justify its operation on specific points on cross-examination when allowed time for checking and research, but it simply was not possible upon the basis of the present record and in the absence of a resolution of other issues in advance to come to any final judgment on Weston's prior accounting except that it is inadequate and must be supplemented and clarified hereafter. The fact that accounting exhibits adduced by the defendants and counterclaimants toward the end of Weston's testimony as somewhat haphazardly compared to some of Weston's accounting results, permitted a plausible though not convincing argument by the attorney for the Gold Technics Defendants that there were insufficiently explained items totaling as much as $800,000.00, could indicate a degree of unwarranted suspicion or a profligacy of contention concerning the nature of Weston's accounting, but it does point up the necessity of further proceedings for an accounting so that the Court can more confidently strike knowledgeable and proper balances based upon the, determinations already made.

125. While I have determined that recovery may not be had against the party Associates on the royalty and development notes and that the funds expended by Cascade and associated interests beyond the $800,000.00 development fund and interest cannot be charged against the party Associates in the accounting, there was not explored at the

trial how such expenditures and funds, or the loans to provide them, should be treated as among the members of the joint venture, which problems are reserved for the accounting.

126. The party Associates contend that Gnolaum Trust, Interphase and Telegraph Mine Limited, Cascade and Weston are the alter egos of each other and that it is necessary in order to prevent fraud or overreaching to disregard the corporate or separate existence between and among them. The foundations for such claim were not fully explored at the trial, particularly with reference to any meaningful separation of corporate entities and structures, although it is clear that Weston controls them all and has utilized others of them as instrumentalities in his projects. Whether it is necessary to disregard any separate corporate existence to preclude fraud or overreching or in the interest of justice can best be determined in connection with the final accounting proceedings. The alter ego issue is therefore reserved for such determination.

127. Cascade's and Weston's assertion of the right to "assess" the Associates beyond their rightful obligations for improper purposes and their initiation of this litigation upon that basis having been determined to be unjustified, willful and in bad faith, the Court will make an award of costs and reason-able attorneys' fees to be determined in amount and allocation in connection with the later accounting proceedings.

V. FAILURE OF PROOF ON OTHER ISSUES

128. Except by the foregoing findings otherwise indicated, the issues of fact raised in the pleadings or reserved in the retrial order are determined against the party or parties having the burden of proof with respect to them, the Court hereby finding that the evidence in support of them

is insufficient.

From the foregoing Findings of Fact, the Court now makes and enters the following:

CONCLUSIONS OF LAW

1. This court has jurisdiction over the subject matter of the action and over the person of each party. Venue is proper.

2. The investment offerings and contracts in question in this case were not securities within the meaning of the Federal, Securities Act of 1933 (15 U.S.C. S 77a-77aa), the Federal Securities and Exchange Act of 1934 (15 U.S.C. S 78a-78hh), or the California Securities Laws (California Corporation Code SS 25,000-25,705), or at all, and their sale to the Associates was not the sale of a security.

3. The contracts involved in or relating to the sale, including the Joint Venture Agreement, were contracts of adhesion to be considered and interpreted in pari materia.

4. None of the parties was guilty of actionable fraud, deceit, misrepresentation, concealment or intentional wrongdoing in the sales of the offering to the Associates, and all proceeded in good faith in reliance upon the reports of the geologists forming a part of the Confidential Memorandum, any omissions, inaccuracies or errors in the Confidential Memorandum being made without intention or scienter or not being material and relied upon by the purchasers.

5. All of the parties entered into the transaction for the purposes of making a profit, with realistic recognition of risks but with a reasonable expectation of profit from their respective investments and there was at the time and under the circumstances then existing a reasonable basis for that expectancy.

6. The September 1980 agreement whereby Rex Mon-

tis acquired thirty-percent interest in the Telegraph Joint Venture in consideration of 480,000 shares of Rex Montis stock was not validly rescinded by the Gold Technics Defendants and the parties should continue to account to each other on the basis of any unpaid purchase price owing by Gold Technics for the original purchase price of its interest and the ownership by Gold Technics of 480,000 shares of Rex Montis stock, which should be deemed held by Rex Montis in trust for Gold Technics and ordered transferred to it

7. The interests of the Associates in the sublease and claim were not assessable and Cascade wilfully and wrongfully maintained that they were.

8. This action, in view of its convoluted nature and the counterclaims and cross-counterclaims, is essentially one in equity calling for the application of equitable principles. Accordingly, the subleases of the party Associates should be deemed expired and terminated, and the party Associates relieved of all liability for unpaid rentals or royalties in consideration thereof, and development costs, whether or not represented by notes heretofore delivered. They are not entitled to return or credit for advance royalty payments already made in cash.

9. No party.is entitled to judgment for alleged defamation, libel, slander or tortious interference with economic advantages or contracts, this Court concluding that any statements that may otherwise have been defamatory were privileged and excusable.

10. The defendants and cross-claimants are entitled to an accounting from the other parties to this action for monies, property, funds or credits coming into their possession and justly belonging to the Defendant Associates and Gold Technics claimants, upon further consideration of quantum meruit and contribution claims with respect to the latter. The respective parties are entitled to judgment for

balances found to be due in accordance with the findings and declarations of the Court and upon such accounting. The Court hereby expressly reserves jurisdiction to require and conduct such accounting, and to enter suitable orders in implementation thereof, including a determination of the extent, if any, to which it would be proper to disregard the separate corporate existence of the so-called Weston corporations to effectuate such accounting and to avoid overreaching, fraud or other injustice under the doctrine of alter ego, and to award attorney's fees and costs.

11. Except as to relief hereinabove mentioned, the issues reserved in the pretrial order or otherwise presented to the Court should be decided against the party or parties having the burden of proof thereon for failure to sustain such burden of proof and for the insufficiency of the evidence to warrant recovery.

12. The pleadings and the pretrial order should be deemed amended to conform to the proof with respect to the relief granted by the Court.

13. Counsel in this action are hereby directed by stipulation or otherwise to jointly or severally prepare and submit to the Court promptly a proposed form or forms of judgment consistent with these amended findings of fact and conclusions of law for consideration by the Court.

14. The submission of a proposed form of judgment in accordance with the foregoing direction will not be deemed in any way to be a waiver of any position heretofore taken by the parties, but simply as an attempt on the part of counsel as officers of the Court to properly implement by judgment the Court's determination, with full reservation of any objections on the part of the parties to the substance of that judgment.

Dated this 3rd day of April, 1985.

A Sherman Christensen,
Senior United States District Judge

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1990

W. DAVID WESTON
Petitioner/Appellant

v.

JEFFREY G. BANKS, ET. AL.,
Defendants

PETITION FOR WRIT OF CERTIORARI

INTERLOCUTORY JUDGMENT
OF THE UNITED STATES DISTRICT COURT FOR
THE DISTRICT OF UTAH CENTRAL DIVISION IN
CASCADE V. BANKS

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH
CENTRAL DIVISION
No. C-82-1223C

CASCADE ENERGY AND METALS CORPORATION,
a Nevada corporation,

Plaintiff ,

v.

JEFFERY G. BANKS, et al,

Defendants

AND RELATED ACTIONS.

HON. A. SHERMAN CHRISTENSEN

The above-entitled matter having come before the Honorable A. Sherman Christensen for trial beginning October 9, 1984, and having continued from day to day, with brief recesses, to and including October 31, 1984; the Court having considered the evidence, the arguments of counsel, documents and pertinent contracts, and having been fully advised in the premises;

JUDGMENT IS HEREBY ENTERED AS FOLLOWS:

1. This Court has jurisdiction over the subject matter of the action and over the person of each party; and venue is proper.

2. The investment offerings and contracts in question in this case are not securities within the meaning of the Federal Securities Act of 1933 (15 U.S.C. SS77a through 77aa), the Federal Securities and Exchange Act of 1934 (15 U.S.C. SS78a through 78hh), or the California Securities Law (California Corporations Code, SS25,000 through 25,705), or otherwise.

3. The sale to the associates, the Joint Operating Agreements, the Working Interest And Sublease Agree-

ments, the Recourse Royalty Notes and the Security Agreements do not constitute a sale of securities under the Federal and California State Securities Law .

4. The Joint Operating Agreements, the Working Interest and Sublease Agreements, the Recourse Royalty Notes and the Security Agreements were contracts of adhesion and must be considered and interpreted in pari materia.

5. The Sublease and Working Interest Agreements, Joint Operating Agreements, Recourse Royalty Notes, Security Agreements, and all other written or oral agreements to which the associates were parties, are expired and terminated; and the party associates are relieved from all liability for unpaid rentals, royalties, loans, or other liabilities under such agreements in consideration thereof. The party associates are not entitled to return or credit for advance royalty payments already made in cash, except as may be indicated by the accounting.

6. The interests of the Associate Parties in the Sublease and Working Interest Agreements, Joint Operating Agreements, Recourse Royalty Notes, and Security Agreements are not and were not assessable. Weston, individually and by and through his office as President of Cascade, willfully, wrongfully, in bad faith and in breach of his fiduciary duties, maintained that the associates' interests in such agreements were assessable.

7. The party associates are hereby awarded their attorneys' fees, costs and expenses against Cascade and Weston in defending this action, in an amount to be determined at the time of the accounting.

8. No party herein made any unjustified or unprivileged defamatory statement, or interfered with any contractual relationship or prospective business advantage of any other party.

9. The September, 1980, agreement whereby Rex

Montis acquired thirty-percent interest in the Telegraph Joint Venture in consideration of 480,000 shares of Rex Montis stock was not validly rescinded by the Gold Technics defendants; and the parties are ordered to continue to account to each other on the basis of any unpaid purchase price owing by Gold Technics for the original purchase price of its interest; and the ownership by Gold Technics of 480,000 shares of Rex Montis stock is deemed held by Rex Montis in trust for Gold Technics and is ordered transferred to it.

10. The defendants and cross-claimants are entitled to an accounting from the other parties to this action for monies, property, funds or credits coming into their possession and justly belonging to the Defendant Associated and Gold Technics claimants, and said accounting is hereby ordered. The respective parties are entitled to judgment for balances found to be due in accordance with the findings and declarations of the Court and upon such accounting. The Court hereby expressly reserves jurisdiction to require and conduct such accounting, and to enter suitable orders in implementation thereof, including a determination of the extent, if any, to which it would be proper to disregard the separate corporate existence of the so-called Weston corporations to effect such accounting and to avoid overreaching, fraud or other injustice under the doctrine of alter ego, and to award attorney's fees and costs.

11. This Interlocutory Judgment shall not be final or appealable unless and until the Court certifies one or more of the issues herein for an interim appeal; and in such event, only those issues so certified shall be appealable.

12. The submission or approval of the form and content of this Interlocutory Judgment shall not be deemed in any way to be a waiver of any rights the parties may have to object or move to amend or supplement the Findings of Fact and Conclusions of Lawor the Interlocutory Judgment

herein, and such parties shall have full reservation of such rights.

DATED this day of , 1985.

BY THE COURT:
HON. A. SHERMAN CHISTENSEN
U.S. District Court Judge